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Royal Commission on Banking and Finance

The Investment Dealers Association
of Canada

Hearings
held at

Ottawa

Vol.

26

Date.

July 11, 1962



Official Reporters
J. J. Aethercut and R. J. Young
Toronto, Ont.



ROYAL COMMISSION ON BANKING

AND FINANCE

Hearings held at Ottawa,
Ontario, on Wednesday,
July 11th, 1962.

THE COMMISSION

The Honourable Dana Harris Porter
Chief Justice of Ontario
Toronto, Ontario - Chairman

Mr. W. Thomas Brown, M.B.E.
Investment Dealer
Vancouver, British Columbia

Mr. James Douglas Gibson, O.B.E.
Banker
Toronto, Ontario

Mr. Gordon L. Harrold
Agriculturalist
Calgary, Alberta

Mr. Paul H. Leman
Corporation Executive
Montreal, Quebec

Mr. John C. MacKeen
Corporation Executive
Halifax, Nova Scotia

Dr. W. A. Mackintosh
Vice-Chancellor
Queen's University
Kingston, Ontario

Mr. H. A. Hampson - Secretary

Mr. Gilles Mercure - Joint Secretary



Ottawa, Ontario,
Wednesday, July 11th, 1962.

--- At 8.45 A.M. the hearing commenced.

SUBMISSION OF THE INVESTMENT DEALERS'
ASSOCIATION OF CANADA

APPEARANCES

Mr. D. S. Beatty	- President, The Investment Dealers' Association of Canada
Mr. Gerald D. Sutton,	- Nesbitt, Thomson and Company Limited
Mr. Andre Leman	- Geoffrion, Robert & Gelinas Co. (Substituting for Mr. F. L. Glasgow, Royal Securities Corporation Limited)
Mr. Clark Kinnear	- W. C. Pitfield & Company Limited
Mr. Harry L. Gassard	- General Manager, The Investment Dealers' Association of Canada
Mr. William Harris	- Harris & Partners Limited
Mr. Noel Fowler	- James Richardson & Sons (Substituting for Mr. N. J. Alexander, James Richardson & Sons)
Mr. J.G.K. Strathy	- Dominion Securities Corporation Limited (Substituting for Mr. T.P.N. Jaffray, Dominion Securities Corporation Limited)
Mr. Alec Adamson	- Clarkson Gordon & Co.
Mr. D. Bruce Shaw	- A. E. Ames & Co. Limited
Mr. Edward H. Ely	- Wood, Gundy & Company Limited
Mr. Grahame Johnson,	- L. G. Beaubien & Co. Limited
Mr. Arthur J. Milner	- Mills, Spence & Co. Limited
Mr. Roland B. Dodwell	- Secretary, The Investment Dealers' Association Brief Committee
Mr. George Cretzianu	- Greenshields Incorporated



1 Mr. Murray D. Cox - Anderson & Company Limited
2 Mr. Howard W. Hunter - Burns Bros. & Denton Limited
3 Mr. R. W. Wadds - McLeod, Young, Weir & Company
4 Limited

5
6 -----
7 THE CHAIRMAN: Call the meeting to order.

8 This morning we have a submission from The
9 Investment Dealers' Association. We have all read the
10 brief that has been filed with us and some, at least,
11 of the supplementary material which has been supplied
12 from time to time and I wish on behalf of the Commission
13 to express our appreciation for the brief and the manner
14 in which it has been prepared. It is quite obvious that
15 a tremendous amount of thought and a great deal of work
16 has been put into this submission and we find it very
17 helpful indeed as it applies to the various matters
18 which are of interest to us.

19 I would expect that it will result in quite
20 a lengthy discussion throughout today and possibly to-
21 morrow so that we may now proceed.

22 Mr. Milner?

23 MR. MILNER: Thank you, Mr. Chairman and
24 members of the Royal Commission.

25 In preparing its brief to the Royal Commission
26 on Banking and Finance, The Investment Dealers'
27 Association of Canada has endeavoured to concentrate its
28 attention on matters which it considers to be of national
29 importance. The recommendations and suggestions derived
30 from its investigations are confined solely to matters which



1 it feels to be in the best interests of Canada.

2 A complete list of the draft recommendations
3 of all committees was distributed to each member firm
4 and the draft summary, together with the supporting
5 evidence, was also made available to members. All
6 members were invited to attend a two-day meeting commencing
7 on May 7th, 1962 to consider these recommendations. This
8 meeting was attended by some 80 members and resulted in
9 eliminating, re-writing and adding recommendations.

10 As you can see from the brief there were
11 some changes made where we deleted certain paragraphs.

12 As a result of this, we feel that the
13 recommendations of this brief truly represent the thinking
14 and opinion, but not necessarily unanimous, of members
15 from coast to coast.

16 To clarify the Association's recommendations,
17 I would like to point out to the Commission the
18 distinction that is intended between the three types
19 of expression used. Where a recommendation is definite,
20 the form "that something be done" is used. Where a
21 suggestion is being advanced to the Commission, the form
22 "that the Commission consider" is used. Where, due
23 to lack of sufficient knowledge or evidence, the
24 Association has not felt itself competent to recommend
25 or suggest action on a subject considered worthy of being
26 brought to the Commission's attention, the form "that the
27 Commission examine" has been used.

28 Several matters have come up for discussion
29 that appeared to relate primarily to the internal operations
30 of the Association or to its relations with other financial



1 associations. These matters have been intentionally left
2 out of the brief because, in our opinion, they were
3 family problems capable of solution by co-operative action.

4 This brief has been prepared on a committee basis
5 and although the changing of the hearing from September
6 to July has made it impossible for some of our committee
7 chairmen to be present, we are fortunate in having most
8 of them here. If it is agreeable to the Commission, I
9 would prefer that the questions be addressed to myself
10 and then I will be in a position to refer them, where neces-
11 sary, to the member of my committee who is in a position
12 to speak most competently on the subject concerned.

13 May I take this opportunity of introducing
14 the chairmen of the various committees who are with me
15 today.

16 Mr. D. S. Beatty, President, The Investment Dealers'

17 Association of Canada

18 Mr. Roland B. Dodwell, who has acted as Secretary to The

19 Investment Dealers' Association Brief Committee

20 Mr. Harry L. Gassard, General Manager, The Investment

21 Dealers' Association of Canada

22 Mr. Alec Adamson, Clarkson Gordon & Company, an Association

23 Auditor whose firm compiled the statistical

24 data as to sales, etc.

25 Mr. Edward H. Ely, Wood, Gundy & Company Limited - and

26 Mr. R. W. Wadds, McLeod, Young, Weir & Company Limited -

27 Finance Department and Federal and Provincial

28 Finance

29 Mr. Murray D. Cox, Anderson & Company Limited -- Bank of

30 Canada



1 Mr. Grahame Johnson, L. G. Beaubien & Co. Limited --

2 Municipal Finance

3 Mr. Gerald D. Sutton, Nesbitt, Thomson and Company Limited --

4 Corporation Finance and Legislation

5 Mr. Howard W. Hunter, Burns Bros. & Denton Limited --

6 Secondary Bond Market

7 Mr. William Harris, Harris & Partners Limited -- Short

8 Term Money Market

9 Mr. D. Bruce Shaw, A. E. Ames & Co. Limited --Chartered

10 Banks and "Near Banks"

11 Mr. Clark Kinnear, W. C. Pitfield & Company Limited --

12 Retailing Stocks and Bonds and Risk Capital

13 Mr. George Cretzlanu, Greenshields Incorporated --

14 Stock Business

15 Mr. Noel Fowler of James Richardson & Sons, Substituting

16 for Mr. N. J. Alexander of James Richardson &

17 Sons -- Mutual Funds

18 Mr. Andre Leman, Geoffrion, Robert & Gelinas Co. --

19 Substituting for Mr. F. L. Glasgow, Royal

20 Securities Corporation Limited -- Financing

21 Small Business

22 Mr. J. G. K. Strathy, Dominion Securities Corporation

23 Limited, Substituting for Mr. T. P. N. Jaffray,

24 Dominion Securities Corporation Limited --

25 Taxation

26 Unfortunately, Mr. Harold Robertson, Mills, Spence & Co.

27 Limited -- Non-Resident Investment -- is unable to be with
28 us today.

29 That is the panel we have with us today,

30 Mr. Chairman.



1 THE CHAIRMAN: Thank you. That is all you
2 wish to submit at the moment?

3 MR. MILNER: That is all.

4 THE CHAIRMAN: So that we may now proceed
5 with the questions.

6 COMMISSIONER LEMAN: Mr. Chairman -- by the
7 way, sometimes we have heard, depending on the acoustics
8 of the room, that some of the people in the audience
9 cannot hear very well so I think we will all have to
10 make sure that our voices are raised high enough so
11 that everyone can hear us. If anyone at any time does
12 not hear any one of us, and particularly me, please
13 raise your hand and I will make sure to raise my voice.

14 Your interesting brief from the beginning
15 gives us a good history of the industry and while we
16 might all think that we know what an investment dealer
17 is, I wonder if it would be possible for the record
18 to have a short catechism type of definition of what
19 is an investment dealer and what his main functions are
20 and what good he does for the economy. Could you
21 supply us with a broad definition?

22 MR. MILNER: I think, Mr. Leman, I will have
23 Mr. Gassard, our Association Managing Director, answer
24 that.

25 MR. GASSARD: Mr. Commissioner, I would say
26 that the investment dealer is primarily a merchant who
27 performs both the function of an agent and the function
28 of a principal and in performing these functions he
29 plays a role in mobilizing capital and we have to direct
30



1 it into socially and economically approved projects.
2 In other words, he is a mechanism for moving capital
3 about. He also plays a role in the decisions that
4 result in the application of capital under our market
5 system.

6 COMMISSIONER LEMAN: Does that contain all
7 the basic distinctions that characterize the industry?
8 There are other types of institutions who do that too,
9 are there not?

10 MR. MILNER: Well, Mr. Leman, I might go
11 further to say that we have 190 odd members in our
12 Association and the figures we submitted on the volume
13 of the secondary market operations and other phases
14 of our industry tend to show that as an industry we
15 are divided really into two parts. There are some
16 30 to 35 firms who are primarily both jobbers and under-
17 writers -- jobber-underwriters and also deal retail at
18 the same time; in other words, one of our large national
19 houses has offices right from Halifax to Vancouver, but
20 those offices of theirs together with the other remaining
21 160 odd members are primarily dealing with the public
22 either as members or as principals or as agents. The
23 main underwriting is done by this relatively small
24 number of our members. Is that what you wanted?

25 COMMISSIONER LEMAN: Well, that touches the
26 subject a little bit. Perhaps we can do with that
27 definition, it always helps. Part of the definition,
28 the distinctive feature that was mentioned was the
29 moving of capital to those who can use that capital.
30 Banks do that too, do they not?



1 MR. MILNER: Yes, a bank has the same function
2 as we have but our industry covers so many phases of
3 the financial business and there are so many specialists
4 in the field, that is, some of our firms specialize
5 in money market securities more than other securities.
6 Some specialize in the sale of mutual funds going to
7 the other extreme and the Association is so complex
8 in its makeup. We have, as you are well aware, a
9 number of what might be called purely stock exchange
10 members who are members of both the stock exchange
11 and our Association. So that to give a specific
12 description of our industry I think is almost impossible.

13 COMMISSIONER BROWN: I think one of the
14 things that is possibly being looked for, Mr. Milner,
15 is the question of providing a market for the fixed
16 income securities and by the provision of such market
17 the industry thereby makes such instruments possible.

18 MR. MILNER: Well, Mr. Brown ----

19 COMMISSIONER BROWN: It is not only the
20 accumulation of this capital or the provision of it
21 to industry; it is also the provision of the secondary
22 market, and this is what differentiates the bonds and
23 debentures from mortgages -- the marketability.

24 MR. MILNER: I will ask Mr. Hunter to answer
25 that second part.

26 MR. HUNTER: Mr. Commissioner, I think we
27 have been probably dwelling on the primary market aspect
28 of things up to now. The secondary market is an area
29 which has been developed for the resale of securities
30 which were originally distributed. People who have



1 bought securities with the intention of holding them
2 find the necessity of selling them suddenly and we,
3 through our vast trading departments, provide the means
4 whereby they can dispose of their holdings and other
5 people who, at the time of issue, were not prepared
6 to buy for one reason or another have an opportunity
7 of coming to the market and having their securities
8 and this does supply the liquidity which is necessary
9 to encourage people to participate in the capital market.

10
11 COMMISSIONER BROWN: That is the point I
12 wanted to bring out.

13 COMMISSIONER LEMAN: Would you say, Mr.
14 Milner, that there were 30 firms that you would class
15 as more wholesale types of firms and the balance would
16 be more primarily engaged in retail work?

17 MR. MILNER: Well, Mr. Leman, we had these
18 industry figures prepared which the members submitted
19 to Clarkson Gordon who are the Association's auditors
20 and they combined all the figures into an industry
21 figure, but in combining those figures we got them to
22 break it down and we took an arbitrary basis on breaking
23 it down -- this is on the secondary market operations --
24 and the arbitrary basis that we took was taking last
25 year by quarters, each quarter of the last year, the
26 number of firms that had an average inventory of \$1 million
27 or over during the entire year of 1961 and there were
28 33 member firms that had that size of an inventory.
29 I am not saying how big the largest one was, I am
30 merely saying that is where we broke it off. You must



1 remember we were most anxious not to have a double set
2 of figures. You will be hearing the Montreal and Toronto
3 stock exchanges some time later and we combined with
4 their organizations so that the firms that report, some
5 60 of our firms are reporting through the stock exchange
6 as a member to the Investment Dealers' Association --
7 am I right, Mr. Adamson? -- about 125 of the firms
8 reported in this group and the pure stock firms reported
9 to the stock exchange so there is no duplication of
10 figures. We hope there is not anyway.

11 COMMISSIONER LEMAN: In paragraph 37 of
12 Section A you have broken down the groups into three
13 types. You call the first type the integrated house,
14 the second type the distributing house, and the third
15 type you say are specialty houses that are specialized
16 and confine their operations to a narrower field. Have
17 you got the number of firms of each type? That was para-
18 graph 37, section A.

19 MR. MILNER: I am going to ask Mr. Gassard
20 to answer that.

21 MR. GASSARD: Well, Mr. Leman, this would
22 be an estimate because there is a great deal of over-
23 lapping and you have to allot firms arbitrarily but by
24 far the larger group would be the distributing houses.
25 We have 191 members and of these we designate 32 as
26 major positioning houses and those would include all
27 the integrated houses so just as an off the top of my
28 head guess I would say there is probably 15 specialty
29 houses and perhaps 15 to 20 integrated houses and the
30 balance might be more accurately described as distributing



1 houses. But even that classification is subject to
2 debate because our business is a sort of ad hoc business
3 and as conditions change you will find that people who
4 do not ordinarily get into the municipal business will
5 become more active in municipals. I would say the
6 great majority of our 191 member firms are distributing
7 houses.

8 COMMISSIONER LEMAN: And, of course, a firm
9 could move from one classification to another.

10 MR. GASSARD: Yes.

11 COMMISSIONER LEMAN: As a matter of fact, why
12 are they in those particular groups? Is it purely a
13 matter of choice or is it the way they are equipped with
14 capital or personnel or what are the basic characteristics
15 of, say, an integrated house? Would it be from the
16 point of view of the capital available to them or the
17 amount of personnel available to them and the other types --
18 what distinguishes them?
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20
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1 MR. MILNER: Mr. Leman, that is a very broad
2 question to ask.

3 The capital requirements that we have
4 instigated in our association were primarily designed
5 to protect the public against any possibility of loss
6 being suffered through dealing with any one of our
7 member firms.

8 A small local house in Regina does not need
9 the same capital that a large house in Toronto or Montreal
10 needs. The limitations on their business does to some
11 degree depend on their capital because we have very strict
12 regulations as to how much inventory or how much liability
13 firms can carry in relation to their working capital.
14 It is a very complicated system of auditing our members
15 so as to be sure they are all solvent at all times.
16 In answer to your question in regard to specialization,
17 some firms have found it simpler to specialize, I would
18 not say necessarily because they have not got sufficient
19 working capital to follow the other method, but I think
20 it would be fair to say that it has great limitations
21 on the amount of capital related to how much business
22 they can do.

23 COMMISSIONER LEMAN: Does the specialization
24 give a firm an advantage in that particular field?

25 MR. MILNER: I would think so, yes, if they
26 specialize in that field. Take, for instance, the firms
27 that want to specialize in the day-to-day market on
28 short-term money; firms for instance such as Traders
29 Finance, I.A.C., General Motors Acceptance and Simpson-
30 Sears, etc., require practically no working capital



1 because their business is done completely without
2 liability; they are acting as straight agents and are
3 paid a commission. Therefore, there are people who
4 specialize in that they would not necessarily guarantee
5 their large positions in the short-term government field.

6 We have a number of smaller firms which do
7 a very large amount of business in what we call
8 commercial paper.

9 COMMISSIONER LEMAN: There are no firms that
10 are specializing in a type of business that the integrated
11 houses do not do? It is not that type of specialization
12 you refer to?

13 MR. MILMER: No, the integrated houses cover
14 the whole field as best they can. Our integrated houses
15 attempt to cover the whole field of business.

16 COMMISSIONER LEMAN: I ask these questions,
17 Mr. Milner, because your industry in a sense is difficult
18 to analyze for one who is not in it, because so far as
19 I know there are not very many, or perhaps there are not
20 any firms among your 191 members who publish statements.

21 MR. MILNER: The only member we have which
22 publishes a financial statement is Merrill Lynch, and
23 it only publishes its American financial statement, not
24 the Canadian.

25 COMMISSIONER LEMAN: This business of publishing
26 statements is more prevalent in the United States, is
27 it not?

28 MR. MILNER: No, there are very few in the
29 United States which publish. The Boston houses have
30 to publish statements because they have limited stock



1 publicly owned. A number of members of the New York
2 Stock Exchange publish a balance sheet, but I know as
3 a matter of fact that any person can demand a statement
4 from a member of their stock exchange.

5 COMMISSIONER LEMAN: That is in the United
6 States?

7 MR. MILNER: That is in the United States,
8 yes.

9 COMMISSIONER LEMAN: We do not have that
10 regulation here?.

11 MR. MILNER: We do not have that regulation
12 here either in our end of the business or the stock end
13 of the business. That is, members of the stock exchanges
14 in either Montreal or Toronto are not required to
15 submit statements to the public.

16 COMMISSIONER LEMAN: I wonder why there is
17 this reluctance to publish statements in Canada?

18 MR. MILNER: I think that is a very easy thing
19 to answer. We are all private companies. There is no
20 public interest in any of the finance companies in
21 Canada. The finance companies, such as our members, have
22 carried on over a period of years in the same way. I
23 think I am right in saying that. There are no statements
24 issued, for instance, by members of the London Stock
25 Exchange. They never publish annual statements in respect
26 to either their profit and loss or their working capital
27 positions. We are not public companies in the same sense
28 that the banks are, or the insurance companies which are
29 publicly owned and therefore of necessity must publish
30 statements.



1 COMMISSIONER LEMAN: I realize that, but I
2 am just wondering what harm it would do. You see, we
3 heard from a group, I think it was the Security
4 Analysts of Toronto, and they came before us and made
5 quite a good presentation of the value of the corporation
6 industrial companies etc., from an investment point of
7 view in making a lot of financial information available
8 to the public. I can understand from an investment
9 standpoint why that would be so useful, but in turn
10 I wonder if it might not help the public a little bit
11 sometimes if they knew who they were dealing with for
12 certain types of business they do with the investment
13 dealers.

14 MR. MILNER: Frankly, Mr. Leman, we do not
15 see any advantage in that. We think that our own
16 internal audit system, or the association audit system
17 is as foolproof as it is possible in so far as keeping
18 our firms solvent, which is the one thing that would
19 worry us tremendously. That is, if we had a failure of
20 one of our members who was not able to meet his obligations.
21 Our position is such that we are large borrowers from
22 the chartered banks, and the chartered banks do not
23 lend money freely without proper security, so that we
24 just do not see any advantage in publishing financial
25 statements.

26 MR. GASSARD: The Analysts' brief only referred
27 to those corporations whose securities were in the hands
28 of the public, not private companies. I think your
29 argument would be more valid if our members' securities
30 were owned by the public.



1 THE CHAIRMAN: Your underwriting end of the
2 business is to distribute securities of other companies
3 than your own which are generally public companies?

4 MR. MILNER: Public companies.

5 THE CHAIRMAN: I suppose a customer has no
6 particular interest in what your financial position is,
7 is that the position you take?

8 MR. SHAW: That is the position we take.

9 COMMISSIONER LEMAN: I suppose if a corporation
10 was going to make an arrangement with you of the under-
11 writing type he could ask to see the financial statement
12 in order to see how responsible a firm he was dealing
13 with?

14 MR. ELY: It has never been the practice.

15 MR. BEATTY: I have never known this to happen,
16 but I have known of corporations to ask a bank to guarantee
17 payments on an underwriting commitment for which the
18 dealer has paid a fee and has to re-assure the bank
19 of his ability to meet the commitment.

20 COMMISSIONER BROWN: Perhaps you might outline
21 in a little more detail the standards the association
22 imposes upon its members in order to ensure protection
23 to the public; the number of audits per year and the
24 number of reports per year which must be made?

25 MR. MILNER: Mr. Adamson, would you answer that?
26 Mr. Adamson is our association auditor in Ontario.

27 MR. ADAMSON: The members are required to
28 report twice yearly to us on their financial positions.
29 We get financial statement twice yearly; one an audit
30 statement and the other a statement prepared by the member



1 himself.

2 COMMISSIONER BROWN: I was thinking perhaps
3 you would go further and explain what the regulations
4 are and what happens if you find that the regulations
5 are not being met.

6 MR. ADAMSON: There are certain capital
7 requirements. We have a formula for establishing capital
8 requirements. In submitting a statement to the association
9 auditor a member is required to calculate what his
10 capital/^{is}and how it measures up against the regulations;
11 whether there is an excess or deficiency, and if there
12 were a deficiency in the capital we auditors would
13 do something about it right away.

14 MR. MILNER: I will also ask Mr. Gassard to
15 give the actual procedure of the method of operation
16 when this situation occurs.

17 MR. GASSARD: The association is concerned
18 mainly with three basic qualities. First, the financial
19 competence and capital; secondly, the nature of the
20 business and, thirdly, the conduct and experience of
21 those who conduct the business. Our financial by-laws
22 operate on the basis of district auditors who examine
23 financial statements periodically. The association
24 approves of a panel of auditors from which the member
25 firms may select their own auditors. These auditors
26 periodically deposit with the district auditors, such
27 as Clarkson-Gordon, a financial statement on four
28 forms, which are deposited with the commission as part
29 of our exhibit. As Mr. Adamson pointed out, these
30 statements are based on a margining formula which



1 requires the firm to have enough capital to margin
2 its outstanding commitments; for instance, the
3 inventory against possible declining value, the receivables
4 and future commitments.

5 This formula took about three years to work
6 out and we are indebted to Clarkson-Gordon for working
7 on it.

8 It is very flexible and it enables a small
9 firm whose capital and whose business does not need
10 so much capital, to get by on our present minimum of
11 \$25,000. It requires a larger firm -- an integrated
12 house -- to have vastly more capital. If the district
13 auditor is disturbed with any condition that is
14 developing in the firm's financial position the
15 chairman of the district has a confidential audit
16 committee to which the district auditor can turn and
17 discuss a member firm by number. The auditor has very
18 wide powers in this connection. The audit committee
19 is also comprised of senior auditors who have had
20 years of experience in both good times and difficult
21 times which matures their judgment.

22 The by-law also provides that if the situation
23 is sent to the audit committee and the auditor is
24 dissatisfied it will be taken to the district
25 committee.

26 That is the financial by-law.

27 COMMISSIONER LEMAN: There are insurance
28 requirements as well?

29 MR. GASSARD: There are insurance requirements
30 and requirements as to proper sets of books with



1 segregation of financial securities properly earmarked,
2 and segregation of clients' credit balances.

3 The formula under which we operate, which is
4 known as the regulations under by-law 8 A, provides
5 that if a firm places so much capital in the business
6 they can conduct a margin business.

7 The impression I want to leave with the
8 Commission is that this is a flexible by-law because,
9 as Mr. Milner pointed out, there are 191 firms, no
10 two alike, so our by-laws have to meet different
11 situations and meet different marketing conditions.

12 MR. MILNER: I might add, Mr. Leman, I think
13 you asked the question -- no, Mr. Brown, I am sorry --
14 that our by-law regulations, the same as the stock
15 exchange by-laws, do require members, not only at the
16 period of audit, but at all times, to be in a capital
17 position sufficient to meet all liabilities, and if a
18 situation develops where a firm gets over-committed
19 in between the audit periods we have a means of
20 subrogating additional capital until the firm recovers
21 from that particular difficulty. This could be from
22 the situation that they have merely taken on something
23 too large for their capital requirement and when that
24 situation is over they are permitted to withdraw that
25 capital and go back to where they were.

26 COMMISSIONER BROWN: Do we gather from that
27 that the auditor at the end of the year certifies
28 that at no time during the year was the working capital
29 less than a certain figures?

30 MR. MILNER: No, the auditor could not certify



1 that, Mr. Brown, because he would have no knowledge
2 of that fact. Our by-laws do require that at all
3 times we are solvent, or solvent according to those
4 figures. There are a number of instances in respect
5 to the dual operation; this is more particularly true
6 to the stock end of our business rather than the bond
7 end, there are numerous firms which supply additional
8 capital to cover their stock commitments over short
9 periods of time.

10 COMMISSIONER BRWON; Before we finish with that
11 point I wonder if you would also like to outline the
12 history of the increase in these requirements as the
13 volume of business grew in the postwar period, because
14 it is indicative of the continuing of the association
15 to make sure that as business grows in volume the
16 minimum requirements are stepped up?

17 MR. MILNER: Well, our original minimum require-
18 ments were \$10,000. That was the original minimum
19 requirement. It was a long process of education in
20 convincing members from coast to coast of the necessity
21 of having sufficient capital in their operations to
22 cover their operations. In our brief we have attempted
23 to state that we do not want to stop anyone joining
24 our association. We welcome as many of the smaller
25 firms as possible. We think that it is in the best
26 interest of the country to have them members of the
27 association, but the requirements have moved up over
28 that period of years as business has increased and
29 as the necessity for having stricter marginal regulations
30 have increased. It is quite conceivable that sometime



1 in the not too distant future the \$25,000 might have
2 to be raised to say \$50,000.

3 COMMISSIONER LEMAN: Mr. Milner, these figures
4 you have quoted starting at \$10,000 some years back
5 and now \$25,000, being the minimum now, that does not
6 mean much to me in relation to a firm say which would
7 take on an underwriting in the millions of dollars.
8 How is this capital related to the business?

9 MR. MILNER: A firm with \$25,000 does not
10 take those liabilities. The firms with \$25,000 are
11 practically entirely retail distributing firms who are
12 not working on a commitment basis, but really operate
13 as agents.

14 MR. BEATTY: This is free working capital
15 after margining.

16 COMMISSIONER LEMAN: Could you describe this
17 for us just a little bit more? Tell us how the
18 capital must be related to the business done, especially
19 in the underwriting field?

20 MR. GASSARD: Mr. Leman, this is a rather
21 complicated thing to answer unless you have the by-law
22 in front of you. It is in our Exhibit file, 8.A,
23 page 405 of the blue book.

24 This by-law, which I said was a margining
25 by-law, and as your inventory goes up you must margin
26 it. For instance let us take bonds on page 408; within
27 six months it is one-tenth of one per cent of the
28 market value; six months to three years it is one point
29 and so on up to twenty years when it is five points.
30 So, if you have an inventory of a million dollars worth



1 of long-term Government of Canada bonds, you must margin
2 that at five points, or five per cent, so the firm
3 would have to have \$50,000 Government capital to
4 margin that, and it must maintain the liquidity
5 requirement which is set out on page 407.



"Each Member shall have and maintain at all times a minimum liquid capital in accordance with the following requirements, namely:

(a) Such liquid capital must be at least \$25,000; and

(b) Such liquid capital must be at least sufficient to provide an adjusted liquid capital equal to the sum of

(1) 2 per cent of the Member's current liabilities or \$50,000 whichever is the less;

(ii) 2 per cent of the Member's adjusted liabilities; and

(iii) such additional amounts, if any, as may be required by Regulation 3.

Subject to Regulation 4, the adjusted liquid capital of a Member which does not deposit all clients' free credit balance in a clients' trust account or which carries margin accounts for clients or which sells securities on an instalment payment plan"

All these factors govern. There you have margin accounts which are carried for clients, partners, directors and shareholders and accounts with other dealers which have not been settled within 25 days, and this applies to securities which the member has contracted to produce and the securities which the member has contracted to sell, except to the extent of those covered by purchase commitments. In other words, every factor in the investment



1 dealer's balance sheet has been weighed so as to speak
2 with a potential loss factor which must be -- his
3 capital must be able to take care of this and leave
4 a margin of safety, so the big firm must have big
5 capital and the small firm may have to get along with
6 \$25,000.

7 COMMISSIONER LEMAN: If the firm underwrites
8 a \$10 million issue and was in the syndicate type of
9 arrangement and keeps \$2 million of the underwriting
10 for itself, say, then is that not the amount of capital
11 you must have at the moment it indicates it is light?

12 MR. GASSARD: On page 409 it says that this
13 is for ten years, and this is a very substantial margin,
14 in my opinion.

15 COMMISSIONER LEMAN: Would that amount to
16 \$200,000?

17 MR. GASSARD: Yes. Mr. Adamson might want
18 to add to that.

19 MR. MILNER: Do you want to add anything
20 further to that?

21 MR. ADAMSON: No.

22 COMMISSIONER LEMAN: I would like to turn
23 now to a slightly different type of question in my mind,
24 and that is the form that opposition takes in the industry,
25 and by relation again to the various types of things we
26 have talked about; the integrated firms, and the dis-
27 tributing firms and the specialty firms. Does competition
28 among them take a different character according to the
29 type of business they do?

30 MR. MILNER: Well, Mr. Leman, I do not know



1 what business there is that has not got competition.
2 Even the aluminum business has a certain amount, I
3 fancy!

4 THE CHAIRMAN: So they claim!

5 MR. MILNER: That is a very broad general
6 type of question that you are asking. I am going to
7 have Mr. Hunter speak to that, who is pretty conversant
8 with the competition in the secondary market operation,
9 which is really where at least 50 per cent of the
10 competition is, if not 75 per cent.

11 MR. HUNTER: Mr. Commissioner, I would like
12 to say that the investment industry appears to attract
13 men who are competitive by nature, and I do not think
14 that they are aggressive only with regard to trying
15 to make a profit, but I think they strive to build
16 businesses of a lasting nature and their desire is to
17 provide their services. Their performance is the
18 yardstick by which their firms are engaged by the public,
19 and this obviously requires a high degree of competition.

20 In our trading operations if we were not
21 highly competitive we would not do any business; some-
22 body else would beat us, so we must be very competitive
23 in that area. Again, in tendering for new issues, if
24 we try to buy those too cheaply we will not do the busi-
25 ness; we have to be highly competitive. We try to
26 specialize in various areas and we try to get the best
27 personnel that we can to do that special work. We spend
28 a lot of money on research so that we feel we are well
29 supported, in our judgment. We spend a lot of money
30 on our accounting and delivery practice and we spend a



1 lot of money on branch operations throughout the country.
2 This all stems from the desire of the people in the
3 businesses to develop a proper image with the public;
4 an image of integrity and a desire to provide the
5 best service possible. I think this is evident in
6 the narrow spreads which exist in the bond market at
7 most times for most actively traded issues.

8 COMMISSIONER LEMAN: In the field of distri-
9 bution, obviously competition would be in a large part
10 based on the sales force; its competence and the number
11 of people they have. Strictly in the underwriting
12 field what form does the competition take? Do you
13 find in general that borrowers will shop around to
14 find an underwriting that will give them the best price?

15 MR. MILNER: Let me ask Mr. Shaw to answer
16 that because he is in the underwriting field.

17 MR. SHAW: Again, Mr. Commissioner, it is
18 a broad question. Basically, I think one has to qualify
19 what an underwriting department in an individual firm
20 is. It is not a compartment of the business with firm
21 boundaries with so many people doing that and nothing
22 that. The underwriting section of any company is a
23 very important function and a function that attracts
24 the attention of the senior people, particularly if
25 you are introducing a new underwriting into your under-
26 writing family.

27 As Mr. Hunter has said, probably our most
28 precious asset is the reputation we enjoy in the financial
29 community, and the reputation that we enjoy with the
30 corporations that we serve and the adjustors that we serve.



1 I think a responsible firm views a new
2 addition to its underwriting family very much as a fond
3 parent might take a look at a suitor for his daughter's
4 hand.

5 A firm's reputation in the underwriting
6 field is built up over a period of years and the firm
7 is judged by the experience and the securities issued
8 from its underwritings in the active market. Every
9 firm is most anxious, if they build up a good reputation,
10 that they avoid introducing a bad act anywhere because
11 that can be very serious and very damaging, so although
12 it is the desire of every house to make as many
13 underwritings as we possibly can, we screen those
14 underwritings with the greatest of care.

15 Further to the competitive elements, every
16 firm is anxious to do as much underwriting as it possibly
17 can of the type that fits their particular ideas and
18 the sort of security that they want to handle, and
19 those ideas may vary from firm to firm; some firms
20 will concentrate entirely on an investment type of
21 security and they will require a long record of earnings
22 and of successful management. Not that they look askance
23 at new ventures, but simply once they have established
24 for themselves a reputation in the field for handling
25 only investment securities, they do not feel that they
26 can endanger their position by going too far afield and
27 getting into more adventuresome fields. Some will
28 specialize in this type of thing and do an extremely
29 good job in most cases. The cases where there is mingling
30



1 of underwritings of investment type securities on the
2 one hand and on a speculative or new venture type of
3 security on the other hand are not too frequent. There
4 is in this area quite a degree of specialization. The
5 competition is there and it manifests itself in many
6 ways and it is basically an established record of that
7 firm being able to do a good distributing job and to
8 maintain a good active market for the securities placed
9 in their hands.

10 COMMISSIONER LEMAN: You said that my question
11 was very broad; I think your answer was even broader!
12 I specifically asked is there evidence that most
13 borrowers do shop around for an underwriting at
14 the lowest possible cost?

15 MR. SHAW: Very little evidence of that.

16 COMMISSIONER BROWN: There is one further
17 point which I have; do these underwritings have a
18 tendency to switch at all?

19 MR. SHAW: I missed that.

20 COMMISSIONER BROWN: Do the underwriting
21 accounts have any tendency to move between houses at all?

22 MR. SHAW: Occasionally that does happen,
23 but the history in the Canadian field is that the firms
24 stay with the -- the corporations stay pretty largely
25 with the underwriting houses with whom they have been
26 associated for many years. We all take cracks at each others
27 accounts, but not frequently successfully.

28 COMMISSIONER LEMAN: Does this reflect a bit
29 of a lack on the part of borrowers; why do they not
30 shop around more?



1 MR. SHAW: Because they are satisfied with
2 the job that is being done for them. Perhaps it is
3 the same reason why you do not shop around for your
4 chartered accountants or your legal consultant.

5 THE CHAIRMAN: Still, in addition to that
6 the borrower looks to the underwriter for advice.

7 MR. SHAW: Yes.

8 THE CHAIRMAN: As to when to hit the market
9 and many other factors; as to what markets to go to,
10 whether to go to the States or Canada in view of the
11 changing situation, and once people become satisfied
12 with the advice of a certain underwriter I would
13 think they would hesitate to change and go to someone
14 whose advice they know little about. Is not that so?
15 That the underwriter is more than a mere underwriter,
16 he is in a sense in an advisory capacity in most cases?

17 MR. SHAW: Very true, Mr. Chairman. You
18 are reminding me of what is important, and one of the
19 most important things is that the underwriter maintains
20 a continuing interest in the affairs of its underwriting
21 clients.

22 COMMISSIONER LEMAN: We are really discussing
23 now the field of competition. Could one integrated
24 firm go to a known large borrower and say, "We could
25 do just as good a job as the fellow who has been
26 doing it for you for the last 15 years. " Is this
27 done a great deal?

28 MR. SHAW: We suspect that that sort of
29 an approach is occasionally made!
30



1 COMMISSIONER LEMAN: In Exhibit C of Section
2 A, the first part of Section A, there is a record there
3 of the movements in and out of the industry between
4 1955 and 1962. Does that reveal anything to us from
5 this angle of competition? You saw how many members
6 moved out of the industry during that period and how
7 many new ones came in, and it seems that 47 have moved
8 out of the industry and 31 new members came in, and there
9 are reasons why they went out.

10 As a matter of fact, among those reasons
11 there is one that puzzles me; it says "Reason for
12 resignation: resigned and later rejoined". That
13 is hardly a reason for resignation; it is more just
14 a fact is it not?

15 MR. MILNER: I will ask Mr. Gassard to answer
16 that because he deals with that.

17 MR. GASSARD: The history of our membership
18 record shows that because we have so many small members,
19 because the investment business is to a very distinct
20 extent dependent on people, personalities, senior dealers,
21 that you will find there is a constant succession of
22 mergers and split-offs and changes of various kinds
23 occurring. One of these two resignations resulted from
24 a western firm becoming affiliated with an eastern
25 house and it was decided that the western firm would
26 resign from the Association. A few months later they
27 decided there were certain interests they wanted to
28 carry on in a separate business, and they reformed the
29 business and applied for membership again. You might
30



1 say that these are just for reasons of business strategy;
2 they found that they could conduct a certain type of
3 business, perhaps a short bond business and at first
4 they thought they would not need the membership, and
5 then they decided that they would like to start over
6 again.

7 COMMISSIONER LEMAN: I notice from this
8 exhibit that for quite a number of cases of going
9 out of business it was a personality problem, the
10 senior partner or the owner of the firm died, or
11 something, but are there cases -- is there evidence
12 of competition here from firms that resigned or
13 went out of the business because it was too tough,
14 the competition was too difficult to meet?

15 MR. MILNER: Well, I think as far as I
16 can recollect I do not think we have ever had a person
17 go out of business because he was forced out of business.
18 Some of them have gone out of business, particularly
19 in the smaller firms where you had one or two partners
20 only, a very small firm, and just using a hypothetical
21 example, where the father, one of the partners, wanted
22 the boy to go into his own business, so he goes into
23 a totally different business and the other one cannot
24 carry on and joins another firm.

25 Conversely to that, every year or nearly
26 every year we see splinter firms being formed from the
27 larger underwriting houses; people leaving the large
28 underwriting houses feeling that they will have a
29 greater opportunity on their own than staying with the
30 large underwriting house or with the large national house



1 and it varies up and down. There have been a number of
2 mergers and there have been a few resignations for
3 reasons that I stated before, where the business simply
4 ceased to exist, but by and large I think we have had
5 surprisingly few people literally go out of the business.

6 COMMISSIONER LEMAN: Does that throw any
7 light on the competitive atmosphere in the industry?

8 MR. MILNER: I would not think so, no.

9 COMMISSIONER LEMAN: Well, there is a reference
10 in the brief to the effect that what you call the retail
11 business is very difficult to carry on. I think it is
12 paragraph 22 in Section A. It says at the end of
13 that paragraph:

14 "Costs of doing business rose steadily
15 during the 1950's and it has become
16 more difficult to carry on a retail
17 business at a profit."

18 MR. MILNER: I will ask Mr. Kinnear to speak
19 on that; that was in his brief and it is on the retailing
20 of securities from the viewpoint of our industry.

21 MR. KINNEAR: I think the reason for that
22 is that the cost of doing business on a retail basis,
23 based on the spreads which are available in competitive
24 selling to the secondary market are so small for an
25 investment dealer to send a salesman out into the rural
26 parts and pay all his expenses, and unless he does a
27 terrific volume it is done more or less at a loss to the
28 firm.

29 Many firms do have a large rural sales force
30 and depend a good deal on the total volume which is done



1 rather than the individual profits per sale.

2 One of the ways many firms get around this
3 is by having men living in so-called rural spots where
4 their cost of doing business is cut down from living,
5 say, in a major spot and going out every week to sell
6 securities and to call on their clients. It is essential
7 in the retail end of our business to make personal calls
8 and many clients like to be called on personally.

9 Now, this is particularly true in certain
10 areas such as the rural parts of Quebec, where clients
11 like to be offered the securities of various municipalities,
12 and so on, and unless you call on them personally it just
13 would not get that business, but I think that by maintaining
14 the broad coverage on clients right across the country,
15 even though part of it is done at a loss, the 98 members
16 are assisting in a widespread ownership of fixed
17 obligations and equities in Canada.

18 Does that answer your question?
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1 COMMISSIONER LEMAN: Yes, except that I would
2 like to relate this to the figures you have given us.
3 In Exhibits A and B of your brief there are some figures
4 about the sales force employed in the industry in Canada,
5 and it shows the personnel data -- Exhibit A, page 26 --
6 and it seems as though the sales staff in the industry
7 has increased somewhat?

8 MR. KINNEAR: That is correct.

9 COMMISSIONER LEMAN: In recent years. Have
10 these been mostly concentrated in the big firms that
11 tend to get bigger?

12 MR. KINNEAR: No, I would say in the first
13 place many firms are looking to the future. They are
14 taking on younger men, training them for managerial
15 and executive positions in the future. One of the
16 training periods for those men is to have some practical
17 experience; that is one reason. Another reason is
18 that many firms -- some of the smaller ones -- have
19 gone extensively into mutual funds and have built their
20 sales force so they can get as broad a coverage as
21 possible. I would think it is the normal growth
22 in the sales force.

23 MR. MILNER: As an example, in the Province of
24 Quebec four years ago there were something like 500
25 registered salesmen within the securities commission
26 in Quebec practically all of whom belonged to the
27 Investment Dealers' Association, in the main -- 80
28 per cent of them did. In the last four years that has
29 gone up by about 10 per cent only in new entries into
30 our business, but in the meantime there are now 3,000



1 registered salesmen in the Province of Quebec, so the
2 other 2,400 are practically all mutual fund salesmen.
3 A number of our houses have gone in for the distributing
4 of mutual funds as an added adjunct to their business.
5 As Mr. Kinnear said, it enables them to keep people
6 in the smaller areas because the profit on the sale
7 of mutual funds compensates them for selling other
8 securities at the same time. There are differences
9 all across the country in the formation in our own
10 industry.

11 I think you would interested in having Mr.
12 Johnson speak to you for a minute on the retail
13 distribution which exists in Quebec, which is the only
14 province it exists in on municipal securities.

15 MR. JOHNSON: In the Province of Quebec,
16 historically the small investors have always been
17 interested in fixed interest obligations starting
18 originally in the form of mortgages usually handled
19 by the local notary, and in more recent years as our
20 industry has expanded they have gone into the purchase
21 of bonds, usually bonds of local interest, and firms
22 such as mine have found that it was good business to
23 establish salesmen throughout the rural areas that
24 were permanently located, not working out of a branch.
25 We found this has been helpful to the local economy
26 in the province because it has created a demand for
27 securities of smaller municipalities and school boards
28 that would have been difficult to sell to institutions
29 or to more sophisticated investors: They like the
30 larger situations where they get a broader annual



1 report from the secretary-treasurer.

2 I think that about covers it.

3 COMMISSIONER LEMAN: What I would like to
4 understand, though, is your reference to the fact that
5 it is costing more and more to handle the retail
6 business. Do you mean literally that the retail business
7 had become less and less profitable in the absolute?

8 MR. KINNEAR: In certain phases. If you
9 are distributing Government of Canada bonds in the
10 rural parts of the country and maintain the same spread
11 you would get in Montreal, Toronto or Winnipeg, it
12 is only natural you can't make very much money because
13 you have your salesmen's travelling expenses, delivery
14 costs and so on. That part of the business is becoming
15 less profitable to investment firms if the prices are
16 competitive, which they are. However, a retail business
17 from coast to coast is essential because you can't
18 do underwritings for new ventures, new companies,
19 and expect to sell them all to the sophisticated
20 investor, and by having a retail organization you can
21 seek out the spots where people would like to invest
22 in a company of that nature.

23 I can give you dozens of examples of under-
24 writings which have been done for various firms where
25 you could not sell part of a fixed obligation to any
26 institutions. You had to seek buyers for it. The
27 institution would come along later, after the company
28 had been more or less seasoned, but not in the initial
29 stage. Therefore, I think it is important that a
30 retail organization be kept healthy for that reason.



Nethercut & Young
Toronto, Ontario

1 THE CHAIRMAN: Does the retail organization,
2 for instance in your firm, devote itself to certain
3 areas in, say, the Province of Quebec, and some other
4 firms might service other areas, or is there an overlapping?

5 MR. KINNEAR: There is competition right through.

6 THE CHAIRMAN: Competition from home to home?

7 MR. KINNEAR: That is correct. I have never
8 heard of firms dividing up the country. It is the
9 opposite.

10 COMMISSIONER LEMAN: On the other hand, in
11 A.32 you show the broad distribution of the number of
12 firms that operate across Canada and those that do not.
13 It does seem like a very few firms seem to be able
14 to afford a real blanketing branch system. I am referring
15 to page 10, "Area Served": 144 firms operate only in
16 one province, and 25 in two provinces, and then you
17 come down to very small figures. How do those firms
18 which operate only in one province, which are by far
19 the largest majority -- they operate only in the big
20 provinces like Ontario and Quebec, or all provinces?

21 MR. KINNEAR: All provinces, but I think there
22 are more in the more populous provinces of Quebec and
23 Ontario. There are smaller firms in all provinces --
24 a great number in British Columbia -- in all the
25 provinces of Canada, and they do largely a retail
26 business in the territory in which they serve. Most
27 of those firms are not underwriters except in a limited
28 sense but they co-operate with the larger firms
29 in distributing underwritings of the larger firms.

30 COMMISSIONER LEMAN: To an underwriting firm good



1 distribution is also very important. Would you suggest
2 that retailing is so little profitable that the big
3 integrated firms make up for that through the underwriting?
4 Is it the underwriting part that provides most of the
5 profit?

6 MR. KINNEAR: Underwriting is an important
7 factor in the profits of the larger firms, but they
8 would not be able to do many of the underwritings unless
9 they themselves had a large retail organization, and
10 possibly we should look at the over-all picture rather
11 than the profit made on one or two or five bonds in
12 a rural area, because if you analyzed that particular
13 sale possibly you come up with a loss.

14 COMMISSIONER MacKEEN: In other words, say
15 you take on an underwriting where you were reasonably
16 sure of selling 80 per cent to institutions, and
17 found difficulty in getting rid of the last 20 per cent:
18 If you have a retail organization behind you, you
19 are pretty sure over a period you can dispose of the
20 whole 100 per cent?

21 MR. KINNEAR: That is correct.

22 MR. GASSARD: May I add also, I have been
23 told by a number of our senior dealers that clienteles
24 have the habit of moving away or dying or changing
25 to the competitor, and unless you are out every week
26 building new names on your list you are not going to
27 be in business too long. The late Mr. Ralph Baker,
28 the General Manager of James Richardson, said they
29 had many accounts on which they lost money, but they
30 did it on the theory that enough of these accounts



1 properly handled would become large enough to become
2 profitable accounts. In other words, they form a sort
3 of a nursery which will grow, which is exactly what
4 many of our dealers did with corporate accounts.

5 MR.MILNER: I will go one step further, Mr.
6 Lemman, to say -- and this is my own personal view --
7 but I would be sure that in Canada we could not have
8 50 national houses; there would be too many national
9 houses for the amount of business available. If we
10 have got roughly between 8 and 10 of our members that
11 you would call national houses -- and by "national
12 houses" we refer to people who go from coast to coast;
13 then there is a second group that have, say, five branches
14 only: Some may not be in British Columbia, or not
15 in Winnipeg, or may not be in Halifax. There are 25
16 members who are in two provinces, but there are a
17 number of large firms -- after all, the only way that
18 money can be made in our industry in the underwriting
19 of corporate securities, if you want to confine it
20 to that end, is in selling the last million. If there
21 is an issue of 15 million the money is all made in
22 the selling of the last million. If you are left with
23 one million you cannot sell, you have had a very
24 unprofitable transaction. Therefore, the large under-
25 writing houses have by necessity been forced to, even
26 though it may not be on a bookkeeping basis -- all
27 their branches might not literally make money, but
28 they do make money in the long run because having those
29 branches enables them to dispose of that hypothetical
30 last 10 per cent.



1 COMMISSIONER LEMAN: But that is a case where
2 it is the underwriting that pays the firm, and they
3 have to have a distribution force to put it out into
4 the public?

5 MR. MILNER: The national houses have to
6 have underwritings. They could not exist without
7 underwritings, but they need the co-operation of all
8 these smaller houses in their selling groups and banking
9 groups -- I am speaking of industrials now -- and if
10 you go on to the provincial financing the same situation
11 exists there, that when the Province of Quebec or the
12 Province of Ontario issue \$50 million worth of securities,
13 there again the successful issue is the one where the
14 whole 50 is sold and not only 45.

15 COMMISSIONER LEMAN: Is it possible to state
16 in quantitative terms what volume it takes to keep
17 a salesman on the road? An insurance company could
18 tell us how much a salesman has to sell in a year in
19 order to make a living and earn something for his
20 employer. Is it possible to measure that in your type
21 of business?

22 MR. MILNER: Let me ask Mr. Ely of Wood Gundy.

23 MR. ELY: It is not an easy question, Mr.
24 Leman, but I would guess that a salesman, if the
25 particular salesman were earning \$10,000 a year he
26 should produce four times that much for his firm,
27 because behind that salesman there would be four to six
28 people: Delivery department, accounting department,
29 research department, trading department -- all the
30 departments that work behind the salesman and service



1 him with prices and telephone calls and, from the
2 accounting standpoint, service him by paying his
3 travelling expenses. My off-the-cuff guess would be
4 he would have to produce four times as much as he
5 makes for his firm for the firm as a whole to break
6 even; that is minimum. In most cases those salesmen
7 are guaranteed a certain minimum, and if they don't stand
8 up to that guarantee over a period of years, a change
9 takes place.

10 COMMISSIONER MACKINTOSH: How much would he
11 have to sell in order to produce the 50 thousand?

12 MR. ELY: That depends entirely upon the type
13 of security he is selling and the profit margin in
14 the security. Let us look at provincial, government
15 and provincial securities: It is a published fact
16 that the underwriting firm, the distributing firm,
17 makes X spread and if he were selling, let us say,
18 Dominion of Canada bonds -- I only refer now to
19 new issues because outstanding issues are traded on
20 a very narrow margin -- as far as new issues are concerned,
21 depending on maturity the spread is, let us say, on
22 average in the longer maturities three-quarters of
23 one per cent, and that is as much as it ever is except
24 on savings loan bonds. That is \$7.50 a thousand,
25 so that fellow has got to sell -- if he sells \$1 million
26 worth, his firm makes \$7,500. So, for him to make
27 \$10,000 he has got to sell in the nature of \$7 million
28 or \$8 million worth of those things in a year with all
29 the attendant expense of doing a retail business.

30 COMMISSIONER LEMAN: This matter of spreads:



1 Does the association have anything to do with the
2 establishment of spreads, say, for underwriting, selling,
3 distributing? Is that all set down, or does each firm
4 when it handles a new issue set that for itself and for
5 the group with which it works?

6 MR. ELY: As far as corporate underwritings
7 are concerned, the particular firm that does the
8 underwriting sets the spread in conjunction with the
9 borrower.

10 COMMISSIONER MACKINTOSH: It is part of the
11 agreement?

12 MR. ELY: It is part of the agreement between
13 the borrower and the dealer, and by mutual negotiation
14 they arrive at what seems to be a proper spread for
15 raising that kind of money. That is in the corporate
16 area. Once you move into the Dominion of Canada,
17 provincials, the spread is set by the borrower. If
18 a Dominion of Canada issue is announced, it is announced
19 to the trade what the spread will be.

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1 In provincial securities some are done by
2 negotiation, some are done by public auction and the
3 winner at public auction decides then what spread he
4 can take over and above his cost commensurate with
5 market conditions. In provincials the spread on a
6 negotiated piece of business is agreed upon and the
7 price to the buyers agreed upon.

8 COMMISSIONER LEMAN: Yes, I understand that.
9 Between the borrower and the public there is a total
10 spread negotiated in the private sector and not
11 negotiated in the public sector but as between the
12 various buyers that are needed in order to get these
13 securities into the hands of the public are there
14 association rules as to how much the selling group
15 will get as compared with the banking group etc., or
16 is that really a matter of private negotiation?

17 MR. ELY: It is really a matter of private
18 negotiation and usage over the years. Let us put it
19 this way: On a provincial issue that has been negotiated
20 to make it simple the gross spread is one per cent.
21 Usually in those negotiated issues the syndicate that
22 negotiates them under the leadership of one manager
23 take a part of that one per cent for taking the complete
24 liability before they start to sell it. In practice
25 that might be one-quarter of one per cent. The remaining
26 three-quarters is paid to the distributing house for
27 placing those securities with the private investor
28 or the institutional investor and out of that three-
29 quarters of one per cent a further commission can be
30 allowed under certain circumstances to sub-agents,



1 casual dealers that are not in the group and trust
2 companies in certain instances where trust companies
3 are allowed under law to take it. Does that answer
4 your question, sir?

5 COMMISSIONER LEMAN: Well, is it fairly fixed
6 or does it vary a lot?

7 MR. ELY: The Association have absolutely
8 nothing to do with controlling that. It is none
9 of their business. They are an association. That
10 is up to the individual dealer or group of dealers who
11 negotiate their deal. The competition is so keen
12 that you just simply cannot overrun a proper normal
13 rule-of-thumb. You just do not make a large commission.
14 If you do you are damaging something; you are either
15 not being fair to the borrower or you are not being
16 fair to the fellow who buys so that this keep your
17 spread down.

18 COMMISSIONER LEMAN: There again I was not
19 thinking of the borrower or the investor; I was
20 thinking of the distribution of the cost as between
21 firms that distribute, firms that sell and firms that
22 underwrite etc., and I am talking about the related
23 amount of spread that they get as between the type of
24 firm and the job they do. That is pretty well fixed
25 too -- how much they get for selling, how much there
26 is for underwriting etc., or does it vary a great deal?

27 MR. ELY: In the case of the large integrated
28 houses they do everything so whatever their percentage
29 interest is in a particular piece of business involved
30 they get the original profit for taking the liability



1 and then they get that portion of the remainder which
2 is their portion in the particular syndicate for
3 distributing.

4 COMMISSIONER LEMAN: There that is the firm
5 that does the whole thing?

6 MR. ELY: That is right.

7 COMMISSIONER LEMAN: But the firm that does
8 not do the whole operation, it gets the same proportion
9 of the total for just selling, doesn't it?

10 MR. ELY: For just selling. The firm that
11 takes no liability and does not underwrite and just
12 sells gets a proportion of the gross and that proportion,
13 while it is not standard, it is pretty well standard.
14 I would guess that the selling firm by and large, if
15 he is in the banking group, probably gets 75 per cent
16 of it. If he is in a selling group he probably gets
17 50 per cent of it.

18 COMMISSIONER LEMAN: So these are about the
19 usual proportions -- about 50 per cent is for selling?

20 MR. ELY: About 50 per cent for selling.
21 A 100 per cent for taking a liability and something
22 in between that for the group at large that may not
23 be applied actually in selling.

24 COMMISSIONER LEMAN: Would that also vary
25 with the type of security that is being distributed?

26 MR. ELY: That would vary.

27 COMMISSIONER LEMAN: In other words there
28 might be securities where the underwriting risk is
29 much less than in the case of others and the selling
30 costs much more?



1 MR. ELY; I do not think the percentages would
2 vary too much but the gross spread might vary according
3 to the type of security you are selling. Just as it
4 is now on Dominion of Canada bonds and not quite as
5 narrow on provincial bonds it gets wider on other
6 types of securities which take a greater effort to sell.
7 I think the same percentages apply.

8 MR. MILNER: It would be very close to the
9 figures Mr. Ely gave that you could say that the house
10 that is distributing with no liability where he was,
11 to use an example, on a provincial bond, he gets
12 one-half of one per cent for selling it. If it was
13 a corporate bond with two points between the spread he
14 would get one per cent for selling it and if it was
15 a preferred stock with three points he would get one
16 and a half for selling.

17 COMMISSIONER LEMAN: Which is still about
18 half.

19 MR. MILNER: About half the total.

20 COMMISSIONER LEMAN: In your annual meetings
21 of the Investment Dealers' Association there has never
22 been any discussion of these relative remunerations
23 for the various functions, there has never been any
24 effort or suggestion made that that might be a matter
25 for the association to deal with?

26 MR. MILNER: Well, Mr. Leman, our Association
27 primarily was formed to do all the things that could
28 be better done as a group rather than individual firms
29 having to do the same type of thing over again. But
30 the Association has never attempted to legislate anything



1 in the way of spreads between firms or underwriting
2 profits or they have never made any effort as an
3 Association to go into whether bank groups are properly
4 formed; in other words, whether there should be a
5 different allocation of banking groups or whether
6 there should be a different allocation of selling groups.
7 Those matters are between the large underwriting syndicates
8 or the underwriting houses and the dealers that join
9 them in their particular issues. The Association does
10 nothing in the way of that type of regulation except
11 the one thing that we do not permit what we call un-
12 conscionable profit. If an underwriting firm tried
13 to take 25 per cent profit on selling something to the
14 public we would take a violent objection. We say
15 that is unfair.

16 MR. GASSARD: In fact, our constitution since
17 the founding of the Association strictly forbids the
18 Association to become involved in the discussion of
19 prices or arrangements or anything tending to restrict
20 competition of trade.

21 COMMISSIONER LEMAN: Would that be a restraint
22 on trade type of thing?

23 MR. GASSARD: It might be so considered, the
24 founding fathers thought.

25 MR. MILNER: I can assure you there is no
26 price fixing in our business.

27 COMMISSIONER BROWN: Could I just re-open
28 one small subject and that is, Mr. Ely suggested that
29 the average salesman's remuneration was approximately
30 25 per cent of the gross. Is this general in the



1 industry? You suggested to make \$10, 000 a firm had
2 to make \$40,000.

3 MR. ELY; It is usual, I believe, amongst
4 most stock exchange houses some of which are members
5 of our association that they would pay their salesmen
6 one-third of the recognized stock exchange commission.

7 COMMISSIONER BROWN: I think that is fixed
8 by the stock exchange, isn't it?

9 MR. ELY: Yes.

10 MR. MILNER: That is the maximum.

11 MR. ELY: As far as fixing the spread of a
12 salesman you are talking about a 25 per cent multiple
13 that I was using?

14 COMMISSIONER BROWN: You used 25 per cent
15 and I merely asked if this was general in the industry.

16 MR. ELY: I do not know that it is general;
17 in point of fact my firm pays considerably less.

18 MR. SHAW: I think what should be clarified
19 is that there are two methods of remunerating salesmen.
20 One is salary or guaranteed return and on top of that
21 is the commission. If you are talking in terms of the
22 total remuneration received by a salesman you are not
23 far from being correct. When you use the figure of
24 25 per cent I think if a salesman made \$10,000 the
25 firm must make \$40,000 so it is something like 20 per cent.
26 That 20 per cent then looks after everything that we
27 pay out to salesmen in the way of take-home pay, whether
28 salary and commission or just commission. If he is on
29 a straight commission this $33\frac{1}{3}$ per cent usage in
30 the stock exchange usually applies when there is virtually



no other remuneration going to the salesman. He may have a drawing account against his one-third of the stock exchange commission but as far as the stock exchange is concerned that one-third represents the full pay-out.

MR. MILNER: It even goes farther than that. Now, just taking it one step farther as far as firms are concerned this is just a matter for each individual firm to make up its own mind, as to how it wants to conduct its business but some of the very large firms pay comparatively high salaries to their sales force and a very low rate of bonus or remuneration above their fixed salaries. The smaller firms, not wanting the liability of the very heavy salary pay-out, if business were not as successful as they hoped it would be have a lower salary scale and a higher commission scale. Some firms even go down to where they have a number of their sales force on no salary. Just as Mr. Shaw pointed out they work completely on commission. They are straight commission salesman. So that our industry figures, with those three factors coming in, make it very difficult to get the industry figure together.

The only way you can really assess it, I think, as far as I am concerned, Mr. Shaw and Mr. Ely have expressed it pretty accurately. If you take those three into consideration, that is, about remuneration, the end pay that goes to the salesman whether he gets it by way of a high commission and a low salary or a low salary and a high commission is about the same.



1 COMMISSIONER BROWN: About 20 per cent?

2 MR. MILNER: 20 to 25 per cent would go to
3 the salesman.

4 COMMISSIONER BROWN: Could you give us the
5 ranges?

6 MR. MILNER: How do you mean?

7 COMMISSIONER BROWN: You have indicated some
8 people pay out on a different basis. Would the range
9 run from 15 to 50 per cent, some firms putting out
10 50 per cent to salesmen?

11 MR. MILNER: I think some of our firms at
12 times have paid out 60 to 65 per cent to salesmen.
13 They have not found it worked out very well. It is
14 too high a percentage of the overhead.

15 COMMISSIONER BROWN: I am asking what the
16 range would be.

17 MR. MILNER: The range would be, I would say,
18 between 10 per cent and 50 per cent.

19 MR. ELY: About 90 per cent would be between
20 20 and 25 per cent. The higher the percentage that
21 is paid out the less likelihood there is of good
22 backing service from salesmen.

23 COMMISSIONER LEMAN: I am a little surprised,
24 though, to hear that there would be a matter of
25 restraint of trade if the industry as such did specify
26 what were the proper remunerations for various functions
27 performed by that industry. If you did anything that
28 would affect the borrower or the investor, then perhaps
29 you could be in trouble with the law but it seems
30 strange you would be in any trouble with the law if,



1 within the industry, you set out certain relative
2 remunerations for the functions performed. I may
3 be wrong.

4 MR. GASSARD: May I just say that the association
5 has on many occasions sponsored open discussions both
6 at our annual meetings and special meetings where
7 various things have been brought up as to how salesmen,
8 for instance, should be remunerated. We act as a
9 forum, not as an adjudicator.

10 COMMISSIONER LEMAN: I certainly do not
11 want to argue about it. I am just looking for facts
12 as to how the industry works. I am not going to argue
13 about it.

14 In your own statistics it looks, on page 26
15 or part 1 of A that it takes on the average three people
16 to back up a salesman. It ranges from 28 per cent
17 sales personnel down to 24 per cent sales personnel
18 for the total, with larger firms 23 per cent. It
19 seems normal the larger firms would have more to back
20 up those salesmen. I suppose that is part of the
21 research staff?

22 MR. ELY: Right.

23 COMMISSIONER LEMAN: Well, in this general
24 section there is just one more question I would like
25 to ask you which is as to the matter of admitting new
26 members into the association. I think Mr. Milner,
27 you mentioned earlier that in order to give everyone
28 a chance to start in the business etc., the capital
29 requirement, subject to any regulation, has not been
30 set too high as a minimum because presumably it was felt



1 it was not necessary to set it too high but how are
2 the admission procedures arranged? Can a firm say:
3 "If I meet these standards I qualify and I will be
4 admitted"? Can anyone join if he wants to by meeting
5 certain very definite standards?

6 MR. MILNER: Well, Mr. Leman, I think I would
7 answer that in a backward way, if I may. What we
8 are trying to do is to upgrade our industry in every
9 possible way we can upgrade it and it is a purely
10 selfish motive, if you want to take it down to the
11 finaly analysis, because every time one of our members
12 does something that contravenes normal business ethics --
13 I am not speaking about criminal offences but business
14 ethics -- the publicity going into the press affects
15 the whole industry. Therefore, we want to be sure
16 that new members coming in appreciate the code of
17 ethics that we feel are necessary to belong to our
18 association and I am going to ask Mr. Gassard to
19 give you the regulations regarding new members but if
20 you bear in mind that the principle is to try to be
21 sure that the members will make good members of our
22 association -- and we go one step farther, we now
23 have a spot audit system that will operate that 10 per
24 cent of our members every year have to break down their
25 sales into categories. We want to be sure that we do
26 not get members who are dealing in nothing but very
27 highly speculative stocks. We do not think they should
28 be members of our association in those circumstances.
29 I think Mr. Gassard can give you very briefly the
30 qualifications.



1 MR. GASSARD: Mr. Chairman, most enquiries
2 about membership reach either our Toronto or Montreal
3 offices or perhaps are addressed to the chairmen of
4 the districts and if it comes to our office we explain
5 the philosophy of the association, something of its
6 standards and requirements and try to point out that
7 membership in the association is a responsibility rather
8 than a privilege.

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1 If they are in earnest about this we ask them to read
2 the by-laws and give them an application form to study
3 which is quite a lengthy document, some six pages,
4 which searches into the antecedents of the qualifications
5 and experience of the firm or partnership which proposes
6 to apply.

7 If they proceed on that basis, the application
8 form is studied by the district committee concerned
9 which looks at the references which the applicant
10 gave -- five references within the Association -- and
11 decides really on two bases aside from capital, and
12 that is character and integrity of the people who
13 are applying which are determined by a form of inquiry,
14 and from experience and ability to conduct an investment
15 type securities business. We have in this last year
16 tried to define our standards more objectively by
17 requiring that the firm agree to conduct an investment
18 type business, but we recognize that in a young growing
19 country like Canada with many resources to be developed,
20 firms must also service the whole portfolio and must
21 be prepared to do some business and accept some orders
22 in perhaps more speculative securities. So, we
23 require that at least 50 per cent of their business
24 and earnings be investment type securities as defined.
25 We define investment securities as all fixed income
26 securities not in default of interest; preferred
27 shares not in arrears of dividends and, common shares,
28 whether or not dividend paying, of demonstrated earning
29 power, and where there is any question as to whether
30 a stock falls in that category the matter comes before



1 the committee and it is settled in a democratic fashion
2 around the committee table. It is not too difficult
3 to get a picture of the member's business.

4 If the committee approves the application
5 the applicant is instructed to send his audited balance
6 sheet to the district auditor who in due course reports
7 upon the member's financial position, and when he signs
8 an application form he undertakes by making a statutory
9 declaration that he has read the by-laws and regulations
10 and will undertake to adhere to them.

11 If this is a new member, every six months
12 for three years he is required to report in some way
13 to the committee so they can follow the type of business
14 that the member is carrying on.

15 In addition to that the national executive
16 at its audit meeting each year elects approximately
17 20 members by lots for an informal check to see if
18 they are adhering to our minimum standards.

19 MR. MILNER: Is that sufficient for your
20 purpose, Mr. Leman?

21 COMMISSIONER LEMAN: I would like to know
22 just a little bit more. Are there statistics in regard
23 to the number of applicants? You give us at page 29,
24 Exhibit C, the fact that there were 31 new members
25 admitted in the Association from 1955 to 1962. Do
26 you have any figures as to how many people applied
27 as compared with the number that were admitted?

28 MR. MILNER: Mr. Gassard, have you any
29 figures on that?

30 MR. GASSARD: No.



1 MR. MILNER: Do you know roughly?

2 MR. GASSARD: I would say there is a trickle
3 of inquiries. To give you a comparable example, we
4 had a caller recently. He was an employee of a member
5 firm. He apparently told his employer that he wanted
6 to enter business for himself. He has only been in the
7 business for four years during which time he has apparently
8 demonstrated an aptitude for the business and has built
9 up a substantial clientele of his own. Being an enter-
10 prising fellow probably he feels he could do better
11 paddling his own canoe. We pointed out to him that
12 under our by-laws he must have five years experience.
13 I think the by-law says that the majority of the directors
14 or the majority of the officers must have been in the
15 business for a minimum of five years. That is to get
16 the basic experience which in a difficult and complex
17 industry can best be learned by trial and error.

18 COMMISSIONER BROWN: Would it be fair to
19 say that rather than having applicants turned down
20 they are dissuaded from putting in an application if
21 it looks as though they might be turned down?

22 MR. GASSARD: We give them the facts and
23 point out that really membership in the Association places
24 quite a heavy burden of responsibility on them. If
25 they are the type we want they seem to come back and
26 press their case. If they are the wrong type from the
27 standpoint of our regulations, that is the last we hear
28 of them.

29 MR. ELY: I think it would be fair to say
30 that if we accepted 31 members in a year we would not have



1 had more than 35 applications.

2 MR. MILNER: That was not in one year.

3 MR. SHAW: At the application stage there
4 would be very few turned down. If they are suitable
5 applicants, and that is established before you get to
6 the application stage, there would be very few turned
7 down. It would not be in the applicant's interest
8 to be turned down, and in most cases it works out that
9 the applicant decides to take the advice from the
10 officers as to what he must do to better qualify him-
11 self before getting to the application stage. In my
12 experience I can think of very, very few cases of an
13 application that has been actually filed and not
14 favourably dealt with.

15 MR. MILNER: Of course, in addition to that,
16 the applicant has to have five sponsors, and there is
17 where the difficulty comes to a person who is of dubious
18 quality. He cannot find five members who will sponsor
19 him so his application never gets as far as the Association.

20 COMMISSIONER LEMAN: Oh, one needs to be
21 sponsored?

22 MR. GASSARD: May I correct that? The word
23 is "references".

24 MR. MILNER: Yes, references, but there are
25 cases where the references will come up and say that
26 they do not think that the applicant is the type of person
27 qualified and it ends there. There are a number of firms
28 which might have started had they had proper qualifications
29 to start with, but they found out in time and never
30 made an application form.



1 COMMISSIONER LEMAN: I see. Perhaps we might
2 break if you wish, Mr. Chairman.

3 THE CHAIRMAN: Have you more questions on
4 this point?

5 COMMISSIONER LEMAN: Well, I was going
6 to change the subject a little bit.

7 THE CHAIRMAN: We will adjourn for about ten
8 minutes.

9 (At this point a short recess was taken.)
10

11 THE CHAIRMAN: We will now resume.

12 COMMISSIONER MACKINTOSH: Mr. Chairman, I
13 have one or two questions I should like to ask relating
14 to Mr. Leman's questions. We were talking about the
15 entrance into the industry and differences between the
16 various houses. Are the big houses in the industry
17 getting bigger and the smaller houses getting fewer,
18 or what is the growth trend of the industry?

19 MR. MILNER: The growth trend, Mr. Mackintosh,
20 and this is a pretty broad statement, indicates that
21 the large houses have not got appreciably bigger in
22 the last five years. Secondary portion of the houses
23 have grown. If you take the eight or ten which you
24 might call national houses and take the remaining
25 24 in that secondary group, that group has grown.
26 In the bottom bracket, the smaller bracket, the personnel
27 has grown but largely for the reason that we were mentioning
28 here before. There is a lot of mutual fund activity among
29 that 120 or 130 remaining members. If you include
30 our stock houses you would have even a greater proportion.



1 Our figure did not include the stock houses because
2 they are reporting directly to the stock exchange.

3 COMMISSIONER MACKINTOSH: Among the smaller
4 group is there much amalgamation going on? Are these
5 smaller houses getting together to make somewhat bigger
6 houses?

7 MR. MILNER: No, the tendency has been
8 more for the smaller houses, or the minimum sized houses
9 to merge with larger houses; witness, for instance,
10 Dawson -- Haniford with Greenshields. There has
11 been that type of amalgamation. There has not been
12 very much of the small houses amalgamating between
13 themselves. I think I am right in that, Mr. Gassard,
14 am I?

15 MR. GASSARD: I am not as sure of that as
16 I was a year ago. I thought that the trend was going
17 to continue, but it sort of came to a stop and I do
18 not know now where we are.

19 MR. BEATTY: We have had one amalgamation
20 and one split-up in the last six months.

21 MR. GASSARD: We do not have the statistics.
22 For instance, these figures we gave in Section A are
23 not sufficient to indicate that trend. One would
24 have to have a longer series than we were able to pro-
25 vide to state anything definite about this trend.
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1 COMMISSIONER MACKINTOSH: For another purpose
2 you give some other figures in Section F on page 8,
3 figures on inventories. They are not very useful for
4 this purpose in that you include far too many houses
5 in each group. You have 33 there and not the number
6 which Mr. Milner spoke and the figures are only for
7 one year. They are just for different dates in the
8 one year. The same figures broken down a bit more
9 would perhaps give a better idea what the distribution
10 was.

11 MR. MILNER: Dr. Mackintosh, let me answer
12 that this way. In providing those figures for the
13 one year it was a fantastically difficult job for the
14 industry on account of the fact that practically no
15 two firms have the same accounting practices or the
16 same way of keeping their own records. Some firms
17 want theirs kept by salesmen and some by securities,
18 and to go back and take them out individually would
19 be a very difficult task, and when it came to going
20 back over two or three years before that we found it
21 impossible to get them, and particularly for the firms
22 that are on IBM; anything on mechanical bookkeeping
23 where you just have a card with a number on it and
24 you have to take each individual card and you have to go
25 back to get it to match the security and it becomes
26 an impossible task to do for any further than the one
27 year.

28 COMMISSIONER MACKINTOSH: I don't know that
29 inventory is the best measure of size and extent of
30 activities in any case; I merely referred to that as it



1 was one table in which this distinction between larger
2 and smaller houses was made. Perhaps you can suggest
3 a more available and suitable measure?

4 MR. MILNER: We can submit to you a breakdown
5 breaking that down further from 33 to 8 and 8 and 25;
6 if you would care to have that we can have those figures
7 submitted.

8 COMMISSIONER MACKINTOSH: I would think that
9 would be useful; we would be very grateful.

10 MR. MILNER: Do you have those figures there,
11 Mr. Adamson?

12 MR. ADAMSON: Yes.

13 MR. MILNER: Would you want them right away,
14 Dr. Mackintosh?

15 COMMISSIONER MACKINTOSH: No.

16 MR. MILNER: We can give you them tonight.

17 COMMISSIONER LEMAN: In the personnel series,
18 which you give us at pages 26 and 28 in A.1, you look
19 at staff and you find that in 1958 -- if we look at
20 the over 100 section -- it was 4400 out of 8600 total
21 personnel, which is about 50 per cent. If we look
22 at 1961 and look at 100 and over, we find we get
23 56, a little over 5600 out of 9300, which is 61 per cent.

24 MR. MILNER: That is what I was saying before,
25 that your middle house, your group just under the
26 national house, has increased and the other ones haven't
27 gone down. There has been a big change in the number
28 of personnel in the 24 houses under the top eight or
29 9 houses. Your percentage goes up to about 60 odd
30 per cent from 50 per cent back three or four years ago.



1 COMMISSIONER LEMAN: This, of course, doesn't
2 cover the whole industry, does it?

3 MR. MILNER: It covers the membership.

4 COMMISSIONER LEMAN: You see, in one case
5 you have 100 and over and in the next case you break
6 it down to ones under 200 and then over 200 and I
7 imagine that you add the two together to get a percentage
8 for 100 and over. How many firms does that represent
9 out of a total membership of 100 and over?

10 MR. MILNER: 18 firms.

11 COMMISSIONER LEMAN: 18 out of 191?

12 MR. MILNER: Your total is 196 firms and
13 that includes all the stock houses in these firms
14 because they were having to do with working capital
15 or profits or anything else, so this is all our members,
16 these tables, and I think you will find when you get
17 the stock exchange brief from the stock exchange people
18 you will see that it will tie into these figures.
19 I am ^{not} sure, but I can find out as to how much increase
20 there was in what we call stock houses or stock members,
21 purely stock members.

22 MR. GASSARD: Mr. Milner's point is borne
23 out by the fact that our 1958 survey showed 18 firms
24 with 100 and over staff and the 1961 figures showed
25 24 firms in that group, so those firms crossed that
26 boundary line.

27 COMMISSIONER LEMAN: This brings me to a point
28 which you make in part 2 of that same section, more
29 specifically paragraph 46 where you register in a sense
30 a complaint about the lack of the available statistics



1 in certain areas of the industry. You indicate some
2 of the difficulties you have about getting adequate
3 statistics and you say, "fiscal-year-ends among our
4 Members fall throughout the calendar year; some
5 firms record sales ...", and you list the particulars.
6 Isn't this an area where the association could do
7 something?

8 MR. MILNER: I will ask Mr. Beatty to speak
9 to that; he is present and is now taking this task
10 on.

11 MR. BEATTY: Mr. Leman, we were very impressed
12 with the value to the association of the preparation
13 of the statistics for this Commission, and at our
14 annual meeting the national executive discussed the
15 continuation of the preparation of such statistics
16 on an annual basis for the use of our membership and
17 decided in favour of it. We also will endeavour to
18 persuade our members as far as possible to standardize
19 the procedures in order to make these statistics more
20 consistent and accurate.

21 Also, at the same time as our preparation
22 for the brief has been taking place, we have entered
23 into efforts with the Dominion Bureau of Statistics
24 to furnish important statistics regarding the capital
25 flow through our industry for them and I believe that
26 this will help our own series as well.

27 Also, we have made available to the Bank
28 of Canada and the Department of Finance and the
29 Dominion Bureau of Statistics our own series which
30 we prepare weekly on the capital flow through the system.



1 We don't feel, however, that these particular statistics
2 are sufficiently well developed to merit their publication,
3 but we are working on them.

4 COMMISSIONER LEMAN: This is what you are
5 referring to in paragraph 56 where you say that this
6 is your intention. Could you specifically say what
7 series, what statistical series you have in mind starting in
8 and maintaining in the future, or is that not quite set
9 yet?

10 MR. BEATTY: It is not quite set yet, other
11 than the fact that the statistical data prepared for
12 the Commission appeared to us to have considerable
13 value and we wish to maintain this on an annual basis.
14 It is much simpler for us to plan in the future the
15 development of statistics than to dig them out in
16 the past. If we know we are going to require them
17 it will be easy for us to keep them up. This relates
18 to capital, profits, the whole series; inventory.

19 COMMISSIONER LEMAN: If we might turn to
20 another subject now, I would like to talk a little bit
21 about underwriting. You describe in the brief what
22 the procedure is for underwriting. Starting first
23 with paragraph A.51 -- it is A.56, rather -- I
24 would like to get a somewhat clearer explanation of
25 exactly what are the normal steps for an underwriting,
26 and this is in the area of corporate underwriting.

27 MR. MILNER: Yes.

28 COMMISSIONER LEMAN: The implication from
29 what I read here is that an underwriting agreement
30 is signed, after which a prospectus and various other



1 documents are prepared. Does that give the impression
2 that the price that the borrower is going to get is
3 fixed before these other steps are taken; is that
4 the proper conclusion?

5 MR. MILNER: Are you referring now to corporate
6 underwriting or referring to underwriting generally,
7 because there are two sections to it.

8 COMMISSIONER LEMAN: Let us start with
9 corporate underwriting.

10 MR. MILNER: It is Appendix E, that is the
11 one which we want on corporate underwriting.

12 COMMISSIONER LEMAN: Yes, there is a description
13 of it in this series in the paragraphs on page 18, 19
14 and 20 of that section.

15 MR. MILNER: I am going to ask Mr. Sutton to
16 speak to that corporate underwriting.

17 MR. SUTTON: Mr. Leman, your question relates
18 to the timing and pricing of an issue, is that right?

19 COMMISSIONER LEMAN: Yes, when the prices
20 are actually fixed. Usually in the discussions between
21 the underwriter and the borrower some indication is
22 given of the area of the price which probably would be
23 utilized -- and which remains in the area -- but
24 the specific price is not established until quite shortly
25 before the issue is filed with the Securities Commission.
26 This is because market conditions can change, of course.

27 COMMISSIONER LEMAN: And that is quite shortly
28 before the issue, a week, or what?

29 MR. SUTTON: No, sometimes it is even a few
30 days, sometimes one day.



1 MR. MILNER: In a nervous market a person
2 is left until the last moment that is possible before
3 coming out with the issue, and the borrower is fully
4 aware, as Mr. Sutton says, that there is a spread --
5 he has agreed, for instance, that his money cost
6 will be somewhere, let us say, between $5\frac{1}{2}$ and $5\frac{3}{4}$ per
7 cent; between a range that would be given at the
8 initial discussions.

9 If during the interval between the discussions
10 and the coming to market, the market changed so it
11 had to go to 6 per cent, the underwriter would have
12 to go back to the corporation and say, "It is impossible
13 to do under the spread we have got now, between $5\frac{1}{2}$
14 and $5\frac{3}{4}$; do you want to go ahead at 6%?" and the
15 answer would be either yes or no, we will go ahead
16 regardless of that. From the underwriters' viewpoint
17 the profit margin remains the same. There is no
18 additional profit no matter where the pricing is.
19 Let us assume there was $2\frac{1}{2}$ points in the business,
20 $2\frac{1}{2}$ per cent, it would be the same $2\frac{1}{2}$ per cent whether
21 there was $5\frac{1}{2}$ selling at 99 or 98, it just comes off
22 the bottom end.

23 COMMISSIONER LEMAN: Provided you sold to both
24 of them?

25 MR. MILNER: Yes, the margin is not increased.
26 in the normal -- the arrangement is made with the --
27 or, the borrower makes the arrangement with the under-
28 writer initially as to what is the proper amount or
29 margin -- or whatever you want to call it -- to issue
30 to the public.



1 COMMISSIONER MACKINTOSH: But if you are
2 moving at the 6 per cent and the issue is over-subscribed
3 and all sold by 10 o'clock in the morning, that is a
4 more profitable operation than if you had priced it
5 very closely and it takes some weeks to clear it all
6 up?

7 MR. MILNER: Yes, that is correct, but the
8 underwriter is taking his best judgment as to the
9 proper price of an issue. An issue that is properly
10 priced, the hope is it will go to a slight premium.
11 The underwriter does not want to see an issue go to
12 a 5 per cent or 6 per cent premium. It just kills
13 the whole distribution. You have got the wrong people
14 owning the issue, and you have the great problem of
15 having to resell it in the secondary market.

16 COMMISSIONER MACKINTOSH: I was not criticizing
17 the procedure. I was just trying to understand.

18 COMMISSIONER LEMAN: In this process of
19 judging the market, what are the tools at the disposal
20 of the underwriter or the manager of the syndicate?
21 There is his judgment, with prevailing prices of bonds
22 of the same quality in the market at the time, but
23 can he do anything more to help his judgment?

24 MR. MILNER: I wish there were, but we live
25 largely by our wits as far as pricing an issue is
26 concerned. We have to try to assess the prevailing
27 market on securities both as to whether we are in a
28 rising market or a falling market, and we have to judge
29 the availability in the market at the time of issue
30 of similar securities of an equal calibre and try to



price it in that range. The fact we are all still in business means that over the course of the years we have been fortunate in pricing more issues correctly than incorrectly. You only go along a certain period if you price them all wrong.

COMMISSIONER LEMAN: To what extent are you allowed to talk to anyone about what they would pay for a bond or for a certain maturity of XYZ company?

MR. MILNER: Well, the large underwriter who is taking a commitment -- let us use a figure: A \$10 million bond issue of a corporate issue: He wants, or his ambition is, to have the large institutions -- the professional buyers have to break the backs of the issue when you get into that size. You cannot sell that issue retail. That type of issue is an issue that institutions -- I am assuming this is for institutional purposes -- and the underwriter during the course of the negotiations discusses with certain of the larger buyers the security they are prepared to bring out, and discusses the rate they are proposing to deal, and those buyers will give an indication, "If it were to come at 98 we would be definitely interested." He has then, not an order, but he has an indication that 98 is a satisfactory price to company A. If companies B, C, D and E all say, "No, we would not even look at it unless it was $97\frac{1}{2}$ ", then he has to reduce the price. If he determines then in his own mind the consensus is that 98 is too high, he will go to that $97\frac{1}{2}$ figure.

COMMISSIONER LEMAN: But that is as far as he can go -- just a rough indication? He can't before



1 actually offering practically get a commitment from
2 anybody?

3 MR. MILNER: Oh, yes; it is quite legal under
4 the Securities Acts to talk to professional buyers
5 prior to an issue being sold to the public, and in some
6 instances you have actually firm orders-- most instances,
7 I would say. I will ask Mr. Sutton to speak to that.

8 MR. SUTTON: Yes, we are allowed to talk to
9 the banks and life companies and trust companies, and
10 of course we can sound out potential buyers in the
11 United States. So, you can get a pretty fair idea
12 of the institution support for an issue before it
13 actually comes out. Sometimes, of course, opinions
14 differ as to what a proper level is, and if the under-
15 writer disagrees with the institution, this is where
16 the retail force comes in.

17 COMMISSIONER LEMAN: This is in the area
18 of corporate finance. It is substantially different
19 for other types of issues, like provincials, say?

20 MR. MILNER: I am going to ask Mr. Ely to
21 speak on that.

22 MR. ELY: Yes, it is substantially different,
23 Mr. Lemman, in connection with provincial issues. You
24 can judge provincial issues and municipal issues very
25 accurately except under most disturbed market conditions,
26 and it is seldom the case where we would discuss with
27 the buyer the pricing of a provincial issue or a municipal
28 issue before coming to market.

29 COMMISSIONER MACKINTOSH: Is that because there
30 is more trading in them?



1 MR. ELY: It is because you measure the value
2 of a provincial or municipal issue by the going rate
3 on the Dominion of Canada bonds, and there exists a
4 reasonable spread between those types of securities,
5 but in addition to that the institutions, who, by and
6 large, buy a fair proportion of what we call high-grade
7 issues -- provincial or municipal issues -- would be
8 inclined to want to buy it at the cheapest price
9 possible, and that is not always a good thing for the
10 borrower. So, we rely on our own judgment to price the
11 issue knowing perfectly well it is a fair price both
12 to the borrower and the person who puts up the money,
13 and also with the realization that if we don't sell
14 a fair percentage to the institutional buyers there
15 is a broad market for that type of security elsewhere,
16 and if we were dictated to by the institutions in all
17 cases the borrower would suffer -- except that there may
18 be an exceptional situation where markets were highly
19 disturbed, and then perhaps you might change the rules.

20 COMMISSIONER LEMAN: To revert to the other
21 factor we were discussing relative to corporate finance,
22 in, say, a provincial issue is an underwriter committed
23 for a longer period before the offering than in the
24 case of a corporation bond, or the other way around?

25 MR. ELY: No, an underwriter would be unwise
26 to commit himself either in a corporate issue or a
27 provincial issue or a large municipal issue except
28 immediately before he comes to the market.

29 COMMISSIONER LEMAN: So, in either case, be
30 it a provincial issue or a corporate issue, the period



1 is very short before offering?

2 MR. ELY: I would say as a general rule you
3 commit yourself on a corporate issue the day before
4 you go to market, and on a provincial issue you
5 commit yourself the day you go to market.

6 COMMISSIONER LEMAN: What happens if you bid
7 when there is a bidding process for, say, a municipal
8 issue? Between the time you have put in your bid
9 and the time you offer -- what length of time -- what
10 interval is that?

11 MR. ELY; About half an hour. We will put
12 in our bid -- say, you are bidding on a provincial issue
13 or a municipal issue, and the bids are called for three
14 o'clock: We would usually send a letter to the borrowing
15 body with no price in it. We would drop that price
16 in maybe an hour ahead of the meeting or half an hour,
17 and in another half an hour we would know whether we
18 had bought it or not and we would be going to market.

19 MR. MILNER: Excuse me for interrupting,
20 Mr. Ely, but just to make sure you have this explanation,
21 Mr. Ely is referring to provincial issues and the top
22 grade of municipal issues such as Toronto, Montreal
23 and that type of security. When you get into the smaller
24 municipals there is often considerable delay after the
25 tender, after you have bought it by public tender, before
26 you can get sufficient data from the municipality to
27 be able to make a proper public offering, particularly
28 on small municipals. You do your utmost to get in
29 advance as much as you can, but there is a delay on
30 municipal issues.



1 MR. ELY: But not of any great duration;
2 it may be a matter of hours.

3 MR. MILNER: It may take a day to get the
4 proper figures.

5 MR. JOHNSON: It may take a day to get your
6 prospectus lined up with the proper statistics, but
7 your salesmen would be offering immediately. There
8 is no prospectus required on a municipal issue, but
9 you often may be subject to a satisfactory prospectus --
10 there would be no delay.

11 MR. MILNER: But there is a delay that occurs
12 if you have not got proper statistics, if he says,
13 "Come back when you have the proper statistics".

14 COMMISSIONER BROWN: I hope there is not a
15 suggestion you are making up your bid without statistics.

16 MR. ELY; By and large, you just don't bid
17 if you haven't got proper statistics.

18 COMMISSIONER GIBSON: Mr. Ely, you say there
19 is a fairly well established differential between
20 Canada bonds and provincials and high-grade municipals:
21 Do these vary much, or are they fairly well set?

22 MR. ELY; They are reasonably well set.
23 They vary under certain circumstances. Perhaps one
24 could say there is a yardstick between comparable
25 maturities of Dominion of Canada and provincials and
26 municipalities of higher grade under certain given
27 market conditions. The variation takes place, either
28 widens or otherwise, according to the conduct of the
29 borrower and the view the investor takes of that
30 borrower.



1 COMMISSIONER GIBSON: So the supply of various
2 kinds of security on the market would make a difference?

3 MR. ELY; Supply and demand always make a
4 difference, and I know you realize that. It could
5 be a worthy provincial borrower might be able to
6 borrow for comparable maturity at one-quarter of one
7 per cent below a comparable Dominion, and he might
8 still be very worthy, but because of the weight of
9 borrowing -- the weight of money he has to raise in a
10 particular time, the spread might be forced -- it might
11 be forced to a wider spread. Yet, on the other hand ,
12 you get the reverse.

13 COMMISSIONER GIBSON: So the area of decision,
14 in making a bid at any given moment, is pretty narrow
15 in range?

16 MR. ELY: Very.

17 COMMISSIONER GIBSON: What sort of thing --
18 one-eighth or one-quarter, when you are trying to
19 figure this out?

20 MR. ELY: I would think as a yardstick perhaps
21 one-quarter of one per cent between Dominion of Canada
22 bonds and worthy provincial borrowers, and perhaps
23 another 15 cents, 25 cents in yield when you step down
24 to the municipal field, depending on the borrower.

25 COMMISSIONER GIBSON: The question I was really
26 getting was, when you make a bid you are thinking in
27 terms of a possible range of price that you bid?

28 MR. ELY: That is right.

29 COMMISSIONER GIBSON: This is a very narrow
30 range?



1 MR. ELY: Very narrow.

2 COMMISSIONER GIBSON: Most of these larger
3 provincial operations are done on a group system?

4 MR. ELY; That is right.

5 COMMISSIONER GIBSON: A syndicate system?

6 MR. ELY: That is right.

7 COMMISSIONER GIBSON: And some of them are
8 bid, though -- what sort of range do you have on the
9 bids where there are bids on a provincial issue?

10 MR. ELY: Most of the larger provinces have
11 found to their satisfaction that it is better to go
12 the negotiated route, but when you get smaller provinces,
13 for example, Prince Edward Island, there would be
14 several bids and the range would be very narrow.

15 COMMISSIONER GIBSON: It would be less than
16 one-eighth of one per cent on yield basis?

17 MR. ELY: Yes.

18 MR. MILNER: Much less.

19 MR. ELY: It would be more in the range of
20 half of one per cent, which would be .05.

21 COMMISSIONER GIBSON: Oh, on price?

22 MR. ELY: On price.

23 MR. MILNER: It would be somewhere about
24 .05 on yield. There could be some very low bid that
25 some person puts in who didn't want them but who
26 wanted to bid.

27 MR. ELY: Or didn't have any real ideas of
28 the value.

29 COMMISSIONER MACKINTOSH: I seem to remember
30 we got complaints from one province who had carried



1 on its business in exemplary fashion and they had
2 great difficulty overcoming the ideas of the industry
3 as to what the spread ought to be on their bonds as
4 compared with other provinces, and the ideas of the
5 institutions as to what quota of their bonds they
6 ought to hold. They felt they got slight reward
7 for 8 or 10 years of right-doing.

8 MR. SHAW: That is quite a long period.

9 MR. ELY; I don't quite understand that
10 question.

11 COMMISSIONER MACKINTOSH: The provinces are
12 not all in the same range?

13 MR. ELY: That is right.

14 COMMISSIONER MACKINTOSH: Is there not a
15 grading among provinces?

16 MR. ELY; The market-place grades them according
17 to their performance.

18 MR. MILNER: You must remember, Dr. Mackintosh,
19 we are only intermediaries between the borrower and
20 the lender, and we have to know, in order to be
21 successful where the lender is willing to lend the
22 money, and if he differentiates between two provinces,
23 possibly wrongly even in our opinion, nevertheless
24 we are forced to abide where we know the bonds can
25 be sold or the price they can be sold at.

26 COMMISSIONER MACKINTOSH: Your answer is
27 that the complaint is against the market?

28 MR. MILNER: We have no control over -- we
29 have a control to this extent, that we are doing our
30 utmost to do business and we are trying to show there



1 is real value in the securities we are offering,
2 but up to a point that is as far as we can go. We
3 cannot force people to buy two securities at an equal
4 price.

5 COMMISSIONER LEMAN: What role can you play,
6 for instance, in improving the market for a province,
7 for a municipality?

8 MR. MILNER: Let me give you an example --
9 this is a concrete example over a period of ten years:
10 We did a very large amount of business in the syndicate
11 we are members of in selling Province of Saskatchewan
12 bonds in the American market, and the province at
13 our instigation prepared a vast amount of statistics
14 and we took the provincial treasurer of the province
15 all around to the various buyers and they discussed
16 it between themselves -- how the province was doing,
17 the explanations -- and that has worked out in a number
18 of instances very favourably. Another way of doing it--
19 speaking still on the American type of distribution --
20 some of our firms have asked a dozen or so of the
21 American treasurers of insurance companies to come up
22 to Canada and have taken them on tours showing them
23 the conditions in the various municipalities and
24 provinces, and that type of what we call sales
25 propaganda, we feel, pays off very handsomely.



1 COMMISSIONER LEMAN: Are there some specific
2 techniques used also? I would like to refer you for
3 a minute to paragraph A.47 at page 16 of the A section.
4 At the end of that paragraph you were there talking
5 about municipal finance and you say:

6 "As long as a municipality is willing
7 to use a negotiated type of under-
8 writing instead of the bid system
9 and the syndicate can prepare a good
10 reception for each new issue".

11 Are there preparation techniques used or what are
12 you referring to there?

13 MR. MILNER: Well, Mr. Leman, let me put
14 it this way: if a smaller municipality brings an
15 issue up for tender, let us say there are ten
16 municipalities coming up for tender during the next
17 ten day's time, and there are 25 firms all intending
18 to tender for these municipalities, the cost of the
19 preparing of the data in order to come to market,
20 if you do not buy one of them it is a dead loss. In
21 other words, all your circulars et cetera are obsolete
22 as you did not buy the issue, but on the negotiated
23 deals where you know you are going to get the issue
24 you keep the statistics completely up to date so that
25 you can enter the market really on a minute's notice.

26 In cities like Toronto, Regina, Ottawa,
27 the syndicate managers of these negotiated deals
28 are always in touch with the municipalities and their
29 information is right up to date, but in smaller ones
30 that is not the case and when you are selling smaller



1 municipalities to professional buyers, speaking now
2 of the insurance companies who are the true professional
3 buyers of municipalities, they will argue with you
4 that with two municipalities there is a difference
5 of a fraction of a percent yield between two municipalities.
6 Now they ever can arrive at whether Guelph or Galt has
7 that fine a distinction I do not know, but they will
8 have certain rules and each one has a different rule.
9 Some people want a large amount of industrial assess-
10 ment; some institutions say: "No, we prefer a large
11 amount of household units, not apartment houses, we
12 like cities with nothing but houses in them", and all
13 those varying factors come into play in the bidding
14 and in the selling, so that in your smaller municipalities
15 there is just as much differentiation until you get
16 down to the ones that are very, very difficult, like
17 your local municipalities in the west particularly --
18 in Saskatchewan, Alberta and Manitoba and you get
19 rural school districts. It is very difficult to obtain
20 the proper statistics for those municipalities in
21 advance.

22 COMMISSIONER LEMAN: Mr. Milner, I asked
23 what could you do and what do you do to "prepare a
24 good reception for each new issue". What are the
25 procedures that prepare a good reception for a new
26 issue? Are you allowed to operate in the secondary
27 market?

28 MR. MILNER: No, there is no secondary
29 market on municipalities, or practically no secondary
30 market on municipalities as such. The buyers of muni-



1 municipalities are buying a rate of interest over a period
2 of years. They mature the bonds in the normal course
3 of events unless there is some very wide spread in market
4 rates in between. But we do our best to educate the
5 buyers of municipalities securities as to their relative
6 worth. I do not think I would go any further than
7 that. That is about as far as we can go. The
8 institutions are the ^{important} ones and it is our knowledge of
9 the requirements that they need that help us in bidding
10 and we can assist the municipalities in preparing
11 reports that are satisfactory to those buyers. We
12 get the local treasurer to give all types of statistical
13 information that is not available in the normal
14 information that they keep for public record.

15 COMMISSIONER LEMAN: So this preparation
16 process you are referring to in this particular para-
17 graph is just a question of preparing a good circular,
18 for instance?

19 MR. MILNER: That is true.

20 COMMISSIONER LEMAN: Nothing in the market
21 as such.

22 MR. MILNER: Nothing in the market.

23 COMMISSIONER LEMAN: Now, we have talked
24 a few minutes ago about the short length of time that
25 a commitment is made before an issue goes to market.
26 In view of the fact that in practically all areas
27 provincial, municipal and corporate, there has been a
28 tendency for borrowings to be larger than they used
29 to be, the sizes and the level of expenditure of each
30 type of borrower -- has the size of underwriting been



1 hampered a little bit by reason of the capital available
2 to the underwriters? Has that been at all a confining
3 problem?

4 MR. BEATTY: The underwriter's own capital?

5 COMMISSIONER LEMAN: Yes.

6 MR. MILNER: No, I do not think by and
7 large -- the underwriters that underwrite securities,
8 in my opinion at least, have sufficient working capital
9 or assets to cover all the liabilities they take on
10 and if the municipalities get too large an issue for
11 one dealer to handle he will join with another dealer
12 or two or three dealers in order to share that liability.

13 COMMISSIONER LEMAN: Well, what impressed
14 me, Mr. Milner, over the years is that in the United
15 States, for instance, for a given size of issue --
16 I am talking about large ones, let us say \$50 million
17 and up -- generally the underwriting group is much
18 larger in the States than it is in Canada. Why is that?
19 I have seen underwritings in the corporate finance
20 field of \$75 million or \$100 million divided among
21 150 underwriting firms whereas in Canada the syndicate
22 groups are never that large, are they?

23 MR. MILNER: No, but, Mr. Leman, if you
24 are referring to the American market, the American
25 market is a far larger market even relatively than ours
26 is and the liability factor is of much more importance
27 in the American market than it is here because they
28 will be bidding there not on your \$50 million or \$60
29 million issue, but on six issues during one week
30 totally \$260 million, so they of necessity must get more



1 and more people into their underwriting groups in order
2 to share that liability.

3 Here in Canada our working capital -- I
4 assume that the working capital of our industry is
5 as high as the corresponding American working capital
6 taking it over the whole range now -- not talking about
7 Morgan-Stanleys -- but just relatively speaking the
8 one phase of having to bid on six issues in one week,
9 the placing of issues in Canada is different from the
10 American market. There is a much broader market.

11 COMMISSIONER LEMAN: Would you say in
12 relation to the capital available to them in the
13 States, relative to the liability that they have
14 on risk at any one time, the relationship is about
15 the same?

16 MR. MILNER: About the same, I should
17 think.

18 COMMISSIONER LEMAN: Due to this number
19 of undertakings or commitments in a short period of time?

20 MR. MILNER: That is correct.

21 COMMISSIONER LEMAN: But would the larger
22 capital in the hands of the underwriter enable the
23 underwriter to take a risk over a longer period of
24 time, for instance?

25 MR. MILNER: I think that the average
26 underwriter in Canada wants to limit his liabilities
27 purposely. He does not want to buy everything that
28 is offered. He is content to do what he regards as
29 his share of the business. There has never been
30 any lack of working capital that has restricted any



1 of the bidding I have seen in Canada.

2 MR. SHAW: I think on that, if I may Mr.
3 Milner, it just is not the same business, to carry
4 any liabilities for any length of time, because your
5 market does change so quickly. The important point
6 is to underwrite your issue and sell it as soon as
7 possible.

8 COMMISSIONER LEMAN: What I am trying to
9 gauge is what the real reason is.

10 MR. SUTTON: The reason is really the
11 change in the market.

12 MR. SHAW: And that is where the losses
13 occur over a period of years, it is in the issues
14 that have been undigested within the normal market
15 period that the normal losses when they do occur
16 can far outrun the margin of safety you provided in
17 your pricing to provide for that risk factor, and
18 that has occurred in all sections of the market
19 in the memories of all of us. We have lost sub-
20 stantial amounts of money in what could be considered
21 good provincial issues which were placed at the time
22 too tightly for the then existing market and before
23 you could get them to the market the market had fallen
24 away from you and you would wind up with losses that
25 would far outrun the profits in that same province
26 over a period of several years of underwriting.

27 COMMISSIONER LEMAN: Is there some difficulty
28 in defining and measuring exactly what one would call
29 losses on underwriting? Is that a clear, precise term
30 or a little vague? In other words, you might have to



1 sell a bond you had paid so much for and sell it at
2 a point or two less. That is a clear loss. You
3 might consider that you had suffered a loss if you
4 carried that bond for a length of time you had not
5 expected to carry it, but are there any statistics
6 on losses on underwritings in the industry?

7 MR. SHAW: There are in the individual
8 companies. I would not think they would be available
9 on an association basis. Each of us knows how we
10 have done at the end of the year on our underwriting
11 business and we would hope that we would keep to a
12 minimum those cases where you did distribute the
13 whole issue at your cost or better. But they do occur
14 and I think it would be a safe statement that in the
15 American market there is much more of a tendency and
16 they have had more of an experience -- which might
17 partially answer your previous question -- where, if
18 the market moves against them they are very quick
19 to take their losses and move out, and it is not at
20 all unusual to see an issue having come out priced
21 at \$99.50 and be some 60 per cent sold and see the
22 last 10 per cent sold 2, 2½ points sometimes below,
23 and these are figures that are crossing our desks
24 all the time. We watch the American operations down
25 there and it is a much more frequent occurrence.

26 COMMISSIONER LEMAN: This occurs much
27 more frequently in the United States than in Canada?

28 MR. SHAW: Yes, perhaps not relatively
29 but we are talking about a 15 to one ratio, if you
30 like, and because of the size of the market, of the



1 complexity of the operation we will see occurrences
2 perhaps more frequently in absolute cases than we
3 would see them here. We do not have such statistical
4 or recording cases here so frequently. The point
5 I am making is that it is not at all unusual as you
6 watch the flow of corporate underwritings in the States
7 in a changing market to learn through your American
8 affiliates that this or that particular issue is
9 being cleaned out well below the issued price. Hope-
10 fully, every time it is the other way.

11 COMMISSIONER LEMAN: Why is this? Is that
12 because they take a longer risk in point of time?
13 Certainly you do not mean to imply that the quality
14 of judgment on the market is worse there than here?

15 MR. BEATTY: It is a question of velocity.

16 MR. SHAW: I would say that in that larger
17 market those cases emerge more frequently than they
18 will in our smaller market operations.

19 COMMISSIONER LEMAN: Might it reflect a
20 somewhat tighter underwriting practice there relative
21 to the market? It must reflect something. I think
22 you said it occurred a great deal more in the United
23 States than it does here. What is the cause?

24 MR. SHAW: May I pursue the answer for a
25 moment, Mr. Milner?

26 MR. MILNER: Certainly.

27 MR. SHAW: Is it not related to what Mr.
28 Milner has said, that at any given time one firm down
29 there can be operating in several fields and the
30 possibilities of error are probably greater than here.



1 We operate much less frequently and we are not forced
2 to take such hurried judgments as might happen down
3 there.

4 MR. MILNER: And there is one other point.
5 There is a very marked difference in those two markets
6 to the extent that in Canada we have a much broader --
7 what we call a retail market. I do not mean to say
8 these are Mrs. Smith's and Mrs. Brown's that are necessarily
9 buying, but you have little funds of various kinds
10 in Canada. In the American market, it relies entirely
11 on institutional demand. They have practically no such
12 thing as retail except for tax-exempt municipals.

13 COMMISSIONER LEMAN: And this type of cus-
14 tomer is a tougher customer to sell and to judge ahead
15 of time than the small retail customer in Canada, is
16 that it?

17 MR. MILNER: Yes, the ordinary smaller
18 buyer in Canada is buying a rate of interest. He
19 wants to invest his money at, call it 6 per cent if you
20 like, and you sell it to him at 6 per cent and he is
21 perfectly satisfied. Your corresponding professional
22 American buyer is working on spreads -- he will say
23 "Rather than pay \$100 for that bond I only think it
24 is worth \$99-3/4" and he will not buy it at \$100.
25 We can distribute a lot of our issues here -- I do not
26 mean to say we are distributing at a false value to
27 the public but the public are not trying to purchase
28 an issue for resale the following morning. Some of
29 our institutions do, but the public as a whole here
30 are what I would call long term investors and in the



1 American market they have no such way of distributing
2 that 20 per cent or 30 per cent of the issue that we
3 have here.

4 COMMISSIONER MACKINTOSH: I do not really
5 believe that the unsophisticated investor is as large
6 a pillar of strength to this industry as is being
7 indicated from time to time.

8 MR. SHAW: Is not the difference you were
9 dwelling upon earlier that here in Canada we are
10 different from our counterparts in the States in that
11 many of our firms are integrated and the underwriting
12 firm has its own distributing organization and that
13 does not occur to anything like that extent in the
14 United States? We can take on a whole issue bolstered
15 by the knowledge that you have a distributing organization
16 through the country through whom you can distribute
17 and place your securities. That does not occur in
18 the United States market. The underwriting used in
19 most cases is to underwrite and distribute to other
20 houses or directly into the institutions and move
21 on to the next and if they are caught with an issue
22 they do not have their own retailing organization to
23 help them place it.

24 COMMISSIONER MACKINTOSH: It all comes back
25 to what Mr. Milner said, does it not, that they have six
26 issues coming up in a week and it pays them better to
27 get on to the next job and make their profit out of
28 that rather than to keep a dead duck around trying
29 to recoup some possible loss there?

30 COMMISSIONER LEMAN: On the other hand, there



1 are more people working at this judgment of the market
2 all the time down there than there are here, and that
3 is probably in proportion to the number of issues going
4 out, is it not?

5 MR.WADDS: There are more people working
6 in the market. There is no question about that, but
7 the sheer velocity of these issues in the United States
8 and the rapidity with which your utilities market,
9 for instance, changes in price is such that overnight
10 a piece of merchandise that looked attractive yesterday
11 could have broken a half a point. People do not want
12 their liabilities to pile up too quickly so they get
13 out and the market changes very rapidly.

14 COMMISSIONER BROWN: The Canadian market
15 to a large extent being a retail market is less
16 sensitive too?

17 MR. WADDS: I would say that is right.
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1 MR. MILNER: Providing that you realize
2 that the word "retail" is not referring to individuals.
3 The retail is what we call not large, or whatever you
4 want to call them -- large institutions. It is the
5 250 small ones under that top 50 that absorb a lot
6 of our securities here.

7 MR. HUNTER: Might I also mention that
8 in the United States market practice seems to be
9 that new issues are bought for cash in most instances
10 whereas on the Canadian market there is a much greater
11 tendency to trade out other securities. The flow of
12 cash here is not as great, and we take over securities
13 quite frequently which people are prepared to sell
14 to buy the new issue and this tends to place the
15 new issue fairly satisfactorily.

16 COMMISSIONER GIBSON: Does this mean that
17 the American investing public have much less taste
18 for fixed income securities than the Canadian investing
19 public?

20 MR. MILNER: Definitely less because they
21 use the tax municipals for their retail accounts.

22 COMMISSIONER GIBSON: Somewhere in these
23 papers it has been pointed out that these are mainly
24 pretty rich people which the tax element supports.
25 I would judge from what you say both in the brief
26 and recently that there is a much broader market
27 among the generally lower income levels for fixed
28 income securities in this country than in the United
29 States. Is that a fair statement?

30 MR. MILNER: I think that is a perfectly



1 true statement, Mr. Gibson. If you go back in history,
2 during the first world war when we started victory loans
3 we were able to finance both wars by public money to
4 a much greater extent than the United States which
5 has no such means of distributing their public debt
6 in the hands of the small people.

7 COMMISSIONER GIBSON: I realize that, but
8 you are really saying it applies to municipal and
9 corporations as well?

10 MR. MILNER: Yes, as well.

11 COMMISSIONER GIBSON: It is not just the
12 distribution that is involved.

13 MR. MILNER: It applies to all fixed
14 interest bearing securities. We have a far greater
15 distribution of fixed interest bearing securities
16 in Canada than they have in the United States, far
17 greater.

18 COMMISSIONER BROWN: Can you give us any
19 theory as to why that is so?

20 MR. MILNER: I think every one might have
21 a theory about it. It is a matter of history, that
22 is what it amounts to. The American public obviously
23 have a different theory of investing money than the
24 Canadian public does.

25 COMMISSIONER GIBSON: Maybe they have more
26 aggressive stockbrokers.

27 MR. MILNER: I think that is probably a
28 fair statement. There has been a lot of criticism
29 in Canada of our being unable to develop our own
30 industries because we cannot raise sufficient risk



1 capital. People will not invest in risk industries.
2 That is probably a very valid criticism. We lack
3 a certain amount of courage, but the truth of it
4 is at the moment at least that we have a much greater
5 proportion of fixed interest bearing securities
6 held by the public in general than they have in the
7 United States.

8 MR. ELY: May I speak on that subject for
9 a moment, Mr. Milner?

10 There is the fundamental reason for this
11 that in United States the government is financed
12 through the medium of setting a price on issues
13 with no commission to the dealers, so therefore
14 no dealers do any public distribution, and why should
15 they? The only time when a dealer participates
16 to any extent in the United States in government
17 issues is when he believes the government has perhaps
18 made a slight error and underpriced it. That is not
19 sound business. In the United States the government
20 does not pay a commission to dealers for the dis-
21 tribution of their issues and therefore they do
22 not get distribution and they did not during the
23 war, so they have lost to themselves a very big
24 public market which we have developed under our
25 system which, in our opinion, is better.

26 COMMISSIONER GIBSON: You would say then
27 it is more than technique which they have in the nature
28 of investment dealer business? It is the difference
29 in the character and attitude of the population which
30 accounts for this?



1 MR. ELY: Well, that character of the
2 population to buy fixed income securities in the United
3 States has not been exploited because of the fact
4 that no commission is paid on government issues.
5 This has been developed in this country to a very
6 marked degree.

7 COMMISSIONER MACKINTOSH: What do the
8 poor Americans do with their money?

9 MR. SHAW: They buy mutual funds.

10 MR. ELY: They buy mutual funds and shares
11 and fixed securities find their way into large pools
12 like insurance companies, banks and trust companies.

13 COMMISSIONER BROWN: And what about the tax
14 free?

15 MR. ELY: The tax free generally finds
16 their way into the trust company where the trust
17 company is handling the affairs of a wealthy person.

18 MR. SHAW: It goes back years to the
19 wartime financing of the first and second wars.
20 During the second war we had victory bonds in the
21 hands of one out of every three of the population.
22 The investment dealer industry organized these
23 campaigns and received remuneration for doing so.
24 In the United States your savings bond programs
25 were handled in quite a different way. In no
26 organized way did they mobilize the dealer industry
27 to place the indebtedness of the federal government
28 with the population. Here we did.

29 COMMISSIONER LEMAN: Is this a form of
30 taxdown there to get all these free services for



1 government issues?

2 MR. SHAW: Perhaps we were forced to do
3 what we did and they were not. It took a real
4 organizational effort on our part to take over our
5 problem of handling the money in the latter part
6 of the first war and the second war. Their larger
7 markets and larger population did not make it necessary.

8 COMMISSIONER LEMAN: Now you described
9 the pattern of how these various types of securities
10 are distributed in the economy in the United States
11 as contrasted with what happens in Canada. Could
12 one base a judgment as to which is the more desirable
13 type of distribution on those facts?

14 MR. SHAW: We think, relating to the age
15 of our economy and stage of development, if you like,
16 that what we have developed here has proven to be
17 very workable. We equally feel that we could
18 not have just borrowed their type of operation
19 because it would not have worked for basic reasons.

20 MR. ELY: The borrowers in Canada would
21 never have been able to get the kind of money that
22 we have been able to raise had we gone their way.

23 COMMISSIONER LEMAN: That might have
24 forced the corporate borrowers more into the equity
25 field?

26 MR. MILNER: Yes, conceivably it could
27 have forced them more into that field. Remember,
28 however, that the United States is a supplier of
29 capital to the world in general and has been a supplier
30



1 for a number of years, ever since the end of the first
2 war. We have been a borrower of capital. We have not
3 had sufficient capital in this country to develop
4 with our own money. We have had to borrow outside
5 the country. You have got the same thing in England
6 even still. There is a surplus of investing money
7 in England looking for investments. Here we are
8 on exactly the reverse foot. We have a surplus
9 of investments but lacking buyers.

10 The development in this distribution market
11 in Canada in my opinion has been one of the greatest
12 things that this country has ever witnessed. I think
13 it has meant that we have financed a lot more of our
14 own internal business than we could have done if
15 we used the American or British methods.

16 COMMISSIONER LEMAN: Yes, but I thought
17 you had mentioned that there was not enough enthusiasm
18 or demand for equities in Canada as a result of people
19 investing in fixed income securities too much.

20 MR. MILNER: Oh, I merely said there were
21 some people who felt that we have not properly developed
22 the risk capital market in this country. A number
23 of people have criticized that Canadians as a whole have
24 not been prone to buy risk securities.

25 I think a perfect example, if you want
26 to put it on a different basis, relates to the complaint
27 for instance among the people in the Maritimes, that
28 the shares of the Bank of Nova Scotia are now spread
29 across the country. The Bank of Nova Scotia was a
30



1 Maritime bank originally, but over the course of the
2 years it all has been redistributed in other parts
3 of Canada merely because the citizens in Nova Scotia
4 apparently were not willing to maintain the investment
5 in their own bank.

6 COMMISSIONER BROWN: Sometimes those
7 people moved out of Nova Scotia.

8 MR.MILNER: Yes, some of them did. There
9 is no doubt that there is a weakness in this whole
10 structure of ours for raising what I would call good
11 risk capital. Now, we have no trouble in raising
12 any amount of money for the really high speculative
13 moose pasture capital.

14 COMMISSIONER BROWN: When you say "we"
15 are you speaking for all the investment dealers?

16 MR. SHAW: Those other people.

17 COMMISSIONER LEMAN: Do you think the I.D.A.
18 members could play a role in correcting this?

19 MR. MILNER: I think we are playing a role.
20 I think if you could analyse our figures as an
21 association, in the past twenty years, you would find
22 the industry as a whole has probably derived 40 per
23 cent of its net profit from selling equity securities
24 whereas twenty years ago it was not even 10 per cent.
25 We have improved tremendously.

26 COMMISSIONER LEMAN: That is the distribution
27 of new issue equity?

28 MR.MILNER: No, not necessarily equity
29 securities as such.
30



1 COMMISSIONER LEMAN: Including the secondary
2 market?

3 MR. MILNER: Oh, yes, secondary market.

4 COMMISSIONER LEMAN: Are there any tax
5 structural problems in the tax field between the two
6 countries that have contributed to this result outside
7 of the special factor of tax exemption on municipals in
8 the United States which we know about? The general
9 structure of taxes is not sufficiently different, is
10 it, to produce that result? In both countries
11 interest in the corporate field for tax purposes
12 is similar?

13 MR. MILNER: Yes.

14 COMMISSIONER LEMAN: The corporate tax
15 levels are quite comparable, so are there any tax
16 features that may have produced the result? There
17 has been the effort in Canada through the 20 per cent
18 tax rate that we know of.

19 MR. MILNER: Our income tax here, if you
20 take it down to the basic fundamentals of the income
21 tax structure, is far higher than the United States
22 income tax, particularly in that bracket of people
23 that can invest money in equity securities. We have,
24 for instance, as an example, that they share theirs
25 with their wives, so the income is cut in half immediately.
26 You simply split it between the two. You do not
27 get the people in the 60 per cent bracket in the United
28 States because they add their wives on to it and cut
29 it down to 30 per cent, and they have higher deductions.
30



1 COMMISSIONER LEMAN: Here you are talking
2 about the tax structure from the point of view of
3 the investors. There is no difference from the point
4 of view of the borrowers, is there?

5 MR. ELY: There is no fundamental difference
6 from the standpoint of the borrower.

7 COMMISSIONER LEMAN: You have pointed out
8 the differences from the point of view of the individual
9 investor.

10 MR. BEATTY: The formation of capital for
11 equity investment took place during periods of low
12 income tax or no income tax and there was not a
13 comparable period here.

14 COMMISSIONER LEMAN: But what Mr. Milner
15 just said seems to argue exactly against the result
16 we have got. If our personal tax structure in your
17 opinion is higher here and if we have the 20 per cent
18 dividend exemption, at least rebate for tax, why do
19 people still have a preference for fixed income
20 securities where they pay more taxes on it?

21 MR. WADDS: I think we might say they
22 are all perhaps accumulating capital in this country
23 which, as Mr. Beatty said, took place many years ago in
24 the United States under a lower tax structure. It
25 is customary to save some money before you put it
26 into equities. The fixed income securities in this
27 country is a medium savings. I do not think we have
28 sufficient free risk capital in the hands of the
29 individuals to generate this vast equity.

30 MR. SUTTON: There has been a change. Mr.



1 Milner mentioned the change in the importance of the
2 equity business to the investment dealers in the
3 last 20 years. I should say most of this has occurred
4 in the last ten years. I think there are perhaps
5 two basic reasons for this. One is that dividend
6 tax credit, and the other is this fact, that we have
7 had a rising stock market and more and more people
8 becoming attracted toward it and putting a higher
9 proportion of their portfolios into it. Both of
10 these have influenced this trend in the last twenty
11 years.

12 COMMISSIONER BROWN: Would it have anything
13 to do with the relative margin of profit on the
14 underwriting of new issues of debt type securities
15 in the two markets?

16 MR. SUTTON: No, I do not think so because
17 your risk is greater on the underwriting of common
18 stocks.

19 COMMISSIONER BROWN: I am speaking about
20 the markets in the United States. Is there a
21 narrow margin on the underwriting of the debt type
22 securities that induces them to take it into institutions?

23 MR. SUTTON: This again is a reflection of
24 the historical trend that Mr. Ely mentioned. The
25 underwriting margin on large debt security in the
26 United States is smaller than in Canada because it
27 is pretty well marketed to institutions. Whereas,
28 here we do have retail institutions where the costs
29 are higher and therefore the margins are higher. In
30



1 stocks, of course, you have commissions established
2 by the stock exchanges. In the case of mutual funds
3 you have your loading charge of 7 or 8 per cent which
4 compensates and enables it then to reach a larger
5 proportion of the population. This trend has been
6 underway in Canada too.

7 MR. SHAW: Is there not a danger in this
8 attitude that the Canadian public is too averse
9 to equities; is there not a danger that this is being
10 a bit overdone? When one looks at the job that has
11 been done in Canada over the past certainly ten years
12 in extending the capital for chartered banks; the
13 large rights issues; the additional equities that
14 have come into the utilities through the rights
15 issues; the general field of rights issues -- when
16 all added together during the past few years that
17 represents a significant addition to the equity
18 holdings in Canada, and the greater part of that
19 responsibility for the distribution has rested within
20 our membership. Sometimes I am inclined to be a
21 little irritated with this suggestion that the
22 Canadian is all debt minded or fixed interest minded
23 and has no proper appreciation of the possibilities
24 of equities.

25 COMMISSIONER BROWN: I think this is something
26 on which we would like to get an opinion expressed.
27 That is, has this historical preference for debt
28 securities in the Canadian individual retail market
29 been a good thing or a poor thing? Has it been in
30 the investors interest or has it not been in the investors



1 interest?

2 MR. MILNER: You are asking a question as
3 to whether we think that it is in the best interest
4 of the country?

5 COMMISSIONER BROWN: There was an indication
6 that it was not a good thing. Let us get an opinion
7 on it.



1 MR. MILNER: I would think as an association
2 in what we feel -- and I don't want to go back to what
3 I said before -- that in a country that is by nature
4 one of development, we haven't got sufficient capital
5 for our own needs. I think we have raised probably
6 as much capital in this country as is humanly possible
7 by the method presently used. I think it has been
8 a very unfortunate method.

9 If we had had the other method -- there is
10 no telling what the public would have said about
11 the other method -- but our savings bank deposits,
12 for instance, are very high here, actual savings bank
13 deposits, people who will not even buy bonds but
14 who will simply leave the money on deposit, and we
15 think that you are right in saying that there is
16 an untapped reservoir of money in this country which
17 might be used possibly to better advantage to further
18 develop the country, but I think that we at least
19 have got the satisfaction of knowing that we have
20 got the money in the hands of the public.

21 There may be quite a change in the investment
22 attitude of the public. We witnessed in the past
23 five years, or we have seen a much greater increase
24 in equity securities amongst the public generally
25 and I think that that will continue, but the beautiful
26 part of it is that we have a backlog of fixed interest
27 bearing securities here which we haven't got in the
28 United States.

29 COMMISSIONER LEMAN: Someone referred to the
30 large pools in the States which are larger than in



1 Canada. Would you say that in proportion to the
2 total of savings available for capital investment in
3 Canada there is a smaller or a larger proportion of
4 pool funds as against individual investment funds?

5 MR. MILNER: There is a smaller proportion in
6 Canada of pool funds.

7 COMMISSIONER LEMAN: A small proportion of
8 the total of this pool in Canada?

9 MR. SUTTON: Do you mean in the hands of
10 institutions?

11 COMMISSIONER LEMAN: In the hands of institutions,
12 pension funds and that sort of institutional investment.

13 MR. MILNER: Mr. Cretzianu, do you want to
14 answer that?

15 MR. CRETZIANU: The study we have tried to
16 make has been hampered by the lack of statistics, but
17 it has seemed to us from the figures we have been able
18 to find that individual investment in equity is not too
19 different in Canada from the United States.

20 Samples of family holdings of equities --
21 granted they are for 1959 -- show that there is about
22 the same proportion of families in the United States
23 holding equities as in Canada and, as has been pointed
24 out, there has been for the past 15 years an increase
25 in the interest by Canadians for equities.

26 There have been several reasons for that;
27 for the 20 per cent dividend tax credit and recently
28 the suppression of the 4 per cent surtax, and I must say
29 that the efforts made by the Investment Dealers' have
30 an effect in getting interest in Canadian equities



1 on their part. This has taken the form, among other
2 things, of a great increase of reserves and in
3 development of encouragement to would-be investors.

4 On the other hand, the figures we have been
5 able to gather on the investment of life insurance
6 companies and of pension funds and trust companies
7 have proven that it is in this sector that the
8 holding of equities is lower in Canada than in the
9 United States. The totals we have produced, which
10 you will find in Appendix J -- are somewhat sketchy
11 and the comparisons are perhaps not all valid, but
12 I think they prove the point that it is in that
13 sector that the holdings of equities is perhaps
14 much lower than in the United States.

15 COMMISSIONER LEMAN: Thank you for that
16 information, but that wasn't exactly the point I was
17 raising. What I was groping for was this; out of
18 the total amount available for investment in the two
19 countries, would you say that there is a higher
20 proportion concentrated into institutions -- pool
21 funds, we call them -- in the States than in Canada,
22 or the other way around? Is the individual investor
23 a larger proportion of the market here than in the
24 States, or vice versa?

25 MR. CRETZIANU: I am afraid I am not able
26 to answer.

27 MR. MILNER: Could we have this question
28 asked this afternoon?

29 THE CHAIRMAN: I think it is about time for
30 an adjournment anyway.



1 COMMISSIONER MACKINTOSH: We would be delighted
2 to have it answered this afternoon.

3 THE CHAIRMAN: We will adjourn now until
4 2.00 o'clock.

5 --- Luncheon Adjournment.
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1 --- On resuming at 2.00 P.M.

2 COMMISSIONER LEMAN: We have no doubt you
3 are probably enjoying this as much as we are, but it
4 would seem we got carried away a little this morning
5 with subjects that do not make the line of questioning
6 too logical, so I would like to get back a bit to
7 the technique of underwriting as such against the
8 results obtained during the last few years in the
9 Canadian market. There are numerous references in
10 your brief to the formation of syndicates among I.D.A.
11 members for underwriting purposes, and I think you
12 describe fairly well for what purpose these syndicates
13 are formed. What governs the choice of partners
14 or members of the syndicate generally?

15 MR. BEATTY: I would like Mr. Ely to field
16 that one.

17 MR. ELY: By and large, Mr. Leman, the things
18 that govern the formation of a syndicate are the
19 financial strength of the members, their ability to
20 distribute the kind of securities that are under
21 discussion for that particular syndicate. When you
22 form an underwriting syndicate you are forming it
23 on a piece of merchandise and you will use different
24 houses for different reasons on different types of
25 merchandise.

26 Would you like to be specific on a certain
27 type of vehicle? Would you like to know how we form
28 a syndicate on a provincial issue or a municipal issue
29 or a corporate issue?

30 COMMISSIONER LEMAN: Well, if your general



1 statement at the beginning was to the effect that
2 it is the distribution ability of the various firms
3 for the particular securities ---

4 MR. ELY: By and large, that is it.

5 COMMISSIONER LEMAN: Very well. However,
6 things are not always static in this industry. Do
7 these syndicates tend to stick or is there some
8 variation from time to time on one issue after another
9 of the same type? Are syndicates formed for each new
10 issue, or do they tend to be traditional?

11 MR. ELY; By and large, they tend to be
12 traditional unless there is good reason to change them,
13 because some of the members have either gained in
14 distributing power or lost some of it, gained in
15 financial stability or lost some of it, and from time
16 to time as the issues are getting larger syndicates
17 have been added to.

18 The best example of that, I think, would be
19 the Province of Quebec. I haven't got the figures
20 at my fingertips, but I think when that syndicate
21 was formed -- I think about three years ago or two
22 years ago -- there were perhaps 30 in the syndicate,
23 and I think it^{is} now nearer 50 -- over 50.

24 COMMISSIONER LEMAN: On this score what I
25 am wondering about is whether there is a bit of
26 a vicious circle involved and the distribution ability
27 of certain firms is the criterion used for their
28 participation in certain syndicates. Does their
29 distribution tend to be helped by the fact they
30 already do belong to certain syndicates, and is it



1 more difficult for someone who does not belong to
2 the best syndicates, who get the best issues, to get
3 the distribution that would qualify them?

4 MR. ELY: I think that is perhaps a good
5 point. By and large, the syndicates that have been
6 put together in the past and which are continuously
7 being put together usually comprise those people
8 who have the criteria I spoke about plus those dealers
9 who normally take liabilities. There is a segment
10 of our industry that carries liabilities at all times
11 and there is a segment that does not. By and large,
12 syndicates are made up of people who normally take
13 liabilities for their own account -- have the financial
14 resources to do so. So, when a syndicate, to use
15 a term, goes on the line to purchase an issue outright,
16 no matter what happens we know that issue will be
17 picked up and the borrower will be paid.

18 COMMISSIONER LEMAN: But the phenomenon I
19 was describing does apply a little bit?

20 MR. ELY: Oh yes, I would be the first one
21 to admit that some traditional things are difficult
22 to break from time to time, but they are broken as
23 time goes on; the emphasis changes; one tries to
24 put the emphasis on the formation of the syndicate
25 being made up of people who today have the financial
26 responsibility.

27 COMMISSIONER LEMAN: And again, this is a
28 field where an individual firm -- it is strictly
29 negotiation? There is no arbitration, there is no
30 form of appeal or anything like that?



1 MR. BEATTY: The Association has no part
2 in this.

3 MR. ELY: It is purely negotiation between
4 the syndicate manager or managers and the firm involved.

5 COMMISSIONER LEMAN: Well, when you belong
6 to a certain syndicate for a certain type of security
7 that has been existing for some time, to what extent
8 are the partners consulted about the price and terms
9 of the issue? Is it generally the manager of the
10 syndicate who determines all this in negotiation with
11 the borrower and then tells the syndicate members
12 what it is there is to distribute and on which they
13 have to take a position? To what extent do they make
14 a specific decision on this particular issue to take
15 their normal participation?

16 MR. ELY: The steps are these: The manager
17 or managers -- and in some cases there are joint
18 managers -- first negotiate with the borrower his
19 money requirements, time of coming to the market
20 and approximate area of price, and then usually --
21 I am now talking about other than corporate issues,
22 although I can go into that any time -- it is then
23 usual to get together the senior members of the
24 syndicate for serious consultation on the amount
25 and the price, and when they are all in agreement
26 that the amount is right and the price is right, then
27 the manager or managers go back to the borrower and
28 negotiate the deal. They then take the whole deal
29 to the entire underwriting group who at that time have
30 their say on the pricing of the issue and the size of



1 it before the final liability is taken.

2 COMMISSIONER LEMAN: This is all done within
3 a matter of hours?

4 MR. ELY: Hours. Sometimes negotiations may
5 go on for some time -- some days ahead of time, between
6 the manager or managers and the borrower, on the one
7 hand the syndicate managers giving the best kind of
8 advice and service to the borrower, and on the other
9 hand perhaps trying to fit the borrower into the
10 proper place in the market so he does not run up
11 against another borrower of similar character or size.

12 COMMISSIONER LEMAN: In a few places in the
13 brief -- and again I haven't got my references at
14 hand -- you have expressed some concern over the
15 quality of the securities that are distributed by
16 firms and you say that you feel a strong responsibility
17 for this sort of thing because your name is tied to
18 various issues that come on the market. Can there
19 be an element of conflict of interests sometimes
20 between your position as an underwriter and your
21 position as a distributor?

22 MR. ELY; I suppose there could be, but the
23 question has seldom arisen because I think we are
24 the intermediary and it would be the view of the
25 dealers, I believe, that if they bring an issue to
26 the market that is properly priced both the buyer
27 and the seller get good value. In some instances
28 we are -- I now move more to corporate issues -- in
29 some instances I think it is the view of the whole
30 industry that there are certain types of corporate



1 securities that are perhaps more suited to certain
2 types of investors and we channel our efforts down
3 that line. There are certain people that really cannot
4 afford to buy at risk. There are others who can and
5 are willing to.

6 COMMISSIONER LEMAN: In short, it is your
7 responsibility, and you accept it all along the line?

8 MR. ELY: We accept those responsibilities.

9 COMMISSIONER LEMAN: Yesterday and the day
10 before we discussed a little bit of this whole system
11 with the Life Officers Association and they expressed
12 a little bit of -- I would not say a complaint, but
13 a little bit of dissatisfaction with the so-called
14 exempt list. How is the exempt list arrived at?
15 Again, you might differentiate between the various
16 types of securities.

17 MR. ELY; There would seldom be any differentiation.
18 An exempt list, as our industry understands it, is made
19 up of all the insurance companies, all the trust
20 companies, all the banks and perhaps in some cases
21 certain other large accounts that are peculiar to
22 that issue. To put it clearer to you, the Workmen's
23 Compensation Board of a province may be on the exempt
24 list for an issue of that province, but it would not
25 be on the exempt/^{list} for the issue of another province
26 and, by and large, an exempt list consists of the
27 institutions I have referred to.

28 COMMISSIONER LEMAN: But as between one issue
29 and another, would there be/^a certain percentage of the
30 issue reserved for the exempt list and a completely



1 different percentage for some other issue?

2 MR. ELY: Yes.

3 COMMISSIONER LEMAN: How do you decide how
4 much to leave -- just your judgment?

5 MR. ELY: From time to time the borrower wants
6 to raise money and it is the job of the dealer to
7 bring about a transaction at the proper level for the
8 borrower and the buyer. At that time -- and it has
9 happened many times -- the so-called exempt institutions
10 may have a different view on the market, may have been
11 putting all their money into mortgages and have no
12 money for bonds. For various reasons they do not
13 support the issue, nor are they interested in the
14 liability that the dealer has. It is not their
15 liability. They support or not as they see fit, so
16 that the amount that one sets aside for the so-called
17 exempt list is modified in almost every issue according
18 to our views on the market and how many the institutions
19 will buy. There have been many occasions when --
20 and provincial issues are a good example -- on a
21 \$50 million issue the institutions, insurance companies
22 in particular, have purchased as little as \$3 million
23 out of the \$50 million issue, and no matter what we
24 have set aside for them they were not the slightest
25 bit interested. It was then our job, knowing we
26 brought the issue to the market at a proper price,
27 to find other buyers, which we do.

28 COMMISSIONER LEMAN: So it is an ad hoc
29 decision in each case?

30 MR. ELY: It is an ad hoc decision, by and



1 large, out of our knowledge.

2 COMMISSIONER LEMAN: Does it have anything
3 to do with the other references you make to the need
4 for the type of distribution that you feel would
5 be desirable to provide a market thereafter?
6 We get the impression from the insurance companies,
7 and I think from your brief too, that the insurance
8 companies in general are not great traders in debt
9 securities?

10 MR. ELY: That is wrong.

11 MR. BEATTY: That is wrong. They are very
12 active.

13 COMMISSIONER LEMAN: Don't you feel a tendency
14 on their part to hold on to securities that seem
15 satisfactory to them until they become shorts?

16 MR. ELY; Not necessarily. If you look
17 at the portfolios of the insurance companies you will
18 see that is not so. It is so in the case of corporate
19 securities, by and large, but not entirely, but in
20 the case of provincial securities it is certainly
21 not so. Without any figures in front of me I would
22 say that insurance companies are not always permanent
23 investors in provincial securities. They are inclined
24 to turn them out to buy something else if they think
25 the price is right.

26 COMMISSIONER LEMAN: They gave us some actual
27 figures to the amount of trading compared to the
28 amount of new investments they make year by year, and
29 they didn't seem to be very high traders.

30 MR. ELY: Were these on an industry basis or



1 an individual company basis?

2 COMMISSIONER LEMAN: On an industry basis.
3 They admitted some of them traded a great deal more
4 than others.

5 MR. JOHNSON: Are they talking about trading
6 at the time of a new issue or between new issues?

7 COMMISSIONER MACKINTOSH: They were speaking
8 of new issues as contrasted with the trading.

9 MR. ELY: You can differentiate between
10 insurance companies, and I think the industry will go
11 along with me that there are some insurance companies
12 that, by and large, the securities they buy they hold;
13 there are other insurance companies that are certainly
14 the opposite.

15 COMMISSIONER MACKINTOSH: This is what they
16 said, that some of them were traders and some were
17 not.

18 MR. ELY: That is true.

19 MR. BEATTY: I believe they were not unanimous
20 in their view as to the desirability of exempt lists
21 as opposed to free operation on the market.

22 COMMISSIONER LEMAN: I think there was a
23 little bit of difference of opinion on that score.

24 COMMISSIONER MACKINTOSH: We don't expect
25 any industry to be unanimous.

26 COMMISSIONER LEMAN: In any event, is it
27 your answer to my original question that from the
28 point of view of distribution it does not have too
29 much importance whether a large percentage of an issue
30 goes to institutions or a smaller percentage from the



1 point of view of the market that will be created
2 thereby later for securities?

3 MR. ELY: No, I don't think so; there is not
4 too much importance. Also, the point I was trying
5 to make is that we could never be in the position of
6 setting aside arbitrarily a percentage of an issue
7 for institutions because as many times as not they
8 would not buy that percentage.

9 COMMISSIONER LEMAN: We will want later to
10 come back again to some more specific features of
11 corporate and municipal and provincial finance on
12 this general subject of the technique of underwriting,
13 and unless there are other questions, I would like
14 to pass on.

15 COMMISSIONER GIBSON: Just one point: How
16 do institutions get on the exempt list? Do they
17 ask to be put on? Who decides?

18 MR. ELY: We decide.

19 COMMISSIONER GIBSON: You simply decide in
20 each individual case?

21 MR. ELY: In some cases there have been --
22 we decide what institution we put on the exempt
23 list and, by and large, we put all insurance companies,
24 all banks, all trust companies and certain other large
25 situations or individual issues.

26 COMMISSIONER GIBSON: And the others are on
27 the ability circumstances?

28 MR. ELY: That is right. Under certain
29 circumstances we have had various people who are not
30 an insurance company or a bank, or maybe a pension fund



1 that has grown big enough that they want to be on
2 an exempt list and they have asked us if we will put
3 them on. By and large, we agree. There are certain
4 large accounts that could almost be considered in
5 the institutional field who do not want to be on
6 the exempt list and have asked us not to put them on.
7 By and large, we agree.

8 COMMISSIONER LEMAN: Who gets the spread there
9 on the bonds or the securities that are sold to the
10 exempt list?

11 MR. ELY: The profit that is made on securities
12 that are sold to an exempt list is divided between the
13 entire underwriting group in proportion to their
14 percentage interest in that group.

15 COMMISSIONER BROWN: Can we clarify that: You
16 said "the entire underwriting group". You mean the
17 banking group?

18 MR. ELY: Yes, I mean the banking group.
19 When I said "underwriting group" I meant the purchase
20 group -- it is really the banking group. There are
21 two groups, usually: A banking group headed by
22 a manager or managers buy the issue. Whatever proportion
23 is sold to the exempt list, the profit on that
24 proportion is given to the complete institution on
25 the basis of their participation in the group and
26 their liability.



1 COMMISSIONER LEMAN: I just approach the
2 next subject a little bit by talking about the conflict
3 of interest. I would like to ask you a few questions
4 now about the amount of regulation in the industry
5 from two points of view and really there will be
6 a further subdivision later about the types of
7 securities. The regulation within the industry, what
8 what we might call self regulation, comes from the
9 industry, does it? You describe in here that
10 this Association does carry out a certain amount of
11 policing work in the industry. Are there statistics
12 available on the amount of disciplinary action that
13 has had to be taken from time to time?

14 MR. GASSARD: The number of cases is
15 certainly small. We have been complimented on
16 many occasions by provincial securities commissions
17 for the handful of cases that appear before them.
18 In fact, I think one commissioner said that he never
19 had had occasion to involve a member of our association
20 in a disciplinary case. If, say, the Ontario Commission
21 receives a complaint from a member of the public, it
22 is then referred to the Association who place it in
23 the hands of the discipline committee.

24 Each district has a discipline committee
25 which is composed of the five immediate past chairmen
26 of the district who are not past presidents of the
27 Association and an appeal from their decision can
28 be taken to the national business conduct committee
29 which is composed of the immediate five past presidents
30 of the Association. The procedure is to lay a charge,



1 permit the accused to attend with counsel, if necessary,
2 hear his defense and ask him questions and then to
3 later consider the evidence and bring down a decision.
4 There is one other thing. I, as the senior permanent
5 official, am an ex officio member of each district
6 discipline committee more or less to hold a watching
7 brief for the president who has certain powers to
8 review district discipline committee decisions where
9 he thinks they are too lenient or too onerous, and
10 then we report back, if the complaint originated with
11 the securities commission, the decision and what
12 action we have taken. But these cases are very,
13 very infrequent. I do not know that I can add
14 much to that, Mr. Leman.

15 COMMISSIONER LEMAN: Are there difficulties
16 arising from the fact that it is the industry that
17 has to do that part of the regulating?

18 MR. GASSARD: In what direction -- the
19 difficulty?

20 COMMISSIONER LEMAN: Well, in the direction
21 of the fact that they have to take action against
22 their own members to a large extent?

23 MR. GASSARD: Well, just as a personal
24 observation I have been very much impressed with the
25 due deliberation and the objectivity with which our
26 committees have approached their work and, of course,
27 we do have our counsel there but, for instance, in
28 Mr. Beatty and Mr. Shaw we have two district chairmen
29 who have presided over such hearings and I think you
30



1 could get their reactions. In other words, you
2 have ten people around a table representing various
3 viewpoints and different types of businesses and they,
4 in my judgment, come out to a pretty reasonable con-
5 clusion on the cases.

6 COMMISSIONER LEMAN: I might make one
7 general remark or question. We have received as
8 supplements to the brief some extracts from the by-
9 laws of the Association and some extracts from the
10 regulations. Is there a good office consolidation
11 type of book containing all this material complete,
12 because I find it a little difficult to read?

13 MR. GASSARD: It is at the printers now
14 and should be available this summer.

15 MR. MILNER: Well, Mr. Leman, at the
16 beginning of starting a year ago in September, the
17 Association changed its entire by-laws on membership
18 and on discipline. That was when these new regulations
19 came in and, of course, changing them to the extent
20 that they were changed it meant that under our regulations
21 we have the power to pass -- the national executive has
22 the power to pass by-laws during the course of the year
23 but they have them ratified at the annual meeting.
24 This is different from the two stock exchanges. The
25 Montreal and Toronto stock exchanges have to have any
26 of their by-laws changed by a meeting of the members
27 only; they cannot do it by the committee passing it
28 temporarily except by resolution and the rewriting of
29 these by-laws was such a big task that we were fully
30 aware that certain changes would have to be made by



1 experience during the year. So that at the annual
2 meeting in June there was a long list of minor changes
3 and that is the reason we have not been able to submit
4 to you the final document with the changes, but it
5 should be ready when?

6 MR. GASSARD: I would say August.

7 MR. MILNER: In the next month you will
8 have a complete list of our by-laws, the two you are
9 interested in, membership and discipline.

10 COMMISSIONER LEMAN: And regulations?

11 MR. GASSARD: Yes.

12 COMMISSIONER LEMAN: That will be the blue
13 book?

14 MR. GASSARD: Yes.

15 THE CHAIRMAN: It is a sort of incorporated
16 body, is it?

17 MR. MILNER: No, we are unincorporated.

18 THE CHAIRMAN: Any person who is not a
19 member would not be prohibited from carrying on the
20 business of an investment dealer if he wished, would he?

21 MR. MILNER: That is correct.

22 THE CHAIRMAN: It is not a closed corporation?

23 MR. MILNER: It is not a closed corporation
24 like the stock exchange. For instance, the Toronto
25 stock exchange is incorporated by private bill and
26 I believe the Montreal stock exchange also.

27 THE CHAIRMAN: Yes, and there are various
28 professional organizations that are given certain
29 privileges by statute. You can only practice medicine
30



1 when you are a member of the Association. Yours is
2 not that sort of organization?

3 MR. MILNER: No.

4 COMMISSIONER LEMAN: Well, that leads to
5 a question, what is the advantage of being a member
6 of the Investment Dealers' Association to exercise
7 the profession except the privilege of putting the
8 fact on your door?

9 MR. MILNER: Well, quite frankly, Mr.
10 Leman, there has been a discussion for the last
11 four or five years as to whether we should not
12 become an incorporated body such as the law societies
13 and medical societies having an actual legal entity.
14 When it started it was my understanding (this goes
15 back 25 or 30 years) that the original conception
16 was it was merely a group of people who got together
17 who were in a similar business and they did not want
18 to run the risk of being something that could be
19 attacked in the courts as an entity. I think it
20 might be a fair statement to say that we might be
21 better off if we had the other type of power that
22 could be granted as a society.

23 Now, we are faced with being unable to
24 say we are the only people who are investment dealers
25 although we have gone as far as to get the co-operation
26 of the securities commissions in the listings, for
27 instance, in telephone directories and that type of
28 thing where we are classified separately from hundreds
29 of other people who might sell anything from real
30 estate up or down.



1 MR. GASSARD: The term "investment dealer"
2 is a defined term under the Ontario Securities Act,
3 as Mr. Porter knows, under the Alberta and Saskatchewan
4 Act. The Quebec Act, while it is very similar to
5 the Ontario Act, does not refer to the term "investment
6 dealer"; it refers to "brokers". So that in those
7 three jurisdictions I have mentioned and now more
8 recently British Columbia jurisdiction, the Investment
9 Dealers' Association perhaps have a better chance or
10 a better environment in which to develop an image in
11 the public mind of the investment dealer as an ethical,
12 competent, professional person who is devoted to the
13 concept of self regulation.

14 In fact, the Ontario Securities Act charges
15 us with certain responsibilities in return for certain
16 privileges and it is our ideal and goal to so comport
17 ourselves that those privileges will remain with us.

18 COMMISSIONER BROWN: Would you outline
19 what those privileges are?

20 MR. GASSARD: Well, basically I think it
21 is correct to say that the investment dealing business
22 as compared to life insurance business or banking
23 business enjoys greater freedom from legislative
24 requirements and we believe that freedom is more
25 likely to be maintained if we so conduct ourselves
26 that we place the interest of our clients in first
27 place and try to develop in our sales staffs and the
28 staffs generally who serve the public an awareness
29 of our obligations in return for the position we have
30



1 been allowed to occupy.

2 COMMISSIONER LEMAN: Are you describing
3 the privileges there or the obligations?

4 MR. GASSARD: Well, they are two sides
5 of the same coin.

6 MR. BEATTY: It is a privilege to the
7 extent that our business is rather a technical one
8 and we feel that we can regulate the ethical conduct
9 of our members far more ably than less informed
10 people who are not aware of the day to day tech-
11 nicalities involved in our business and in maintaining
12 the higher standards than would be possible through
13 government regulation we can create a better image
14 and carry on our business more successfully. To
15 this extent it is a privilege.

16 COMMISSIONER MacKEEN: You might have
17 certain advantages as regards the Bank of Canada,
18 for instance?

19 MR. BEATTY: Yes, it is more a matter
20 of practice than legal regulation.

21 COMMISSIONER LEMAN: Well, in the policing
22 area, how is it done? What methods are used? Is
23 there a systematic form of policing work done or do
24 the staff of the commission just wait until there
25 are complaints or reports of unethical practices
26 and bring cases? How do these cases come to your
27 attention -- from complaints from the public or one
28 member telling on another, or what?

29 MR. BEATTY: They come from complaints
30



1 from the public, complaints from securities commissions
2 and from periodic spot checks of the nature of the
3 business of our members. Earlier we told you that
4 20 per cent of our membership reported each year
5 on the nature of their business. Such cases would
6 come to light through these periodic checks. They
7 could come up through the audit committee.

8 COMMISSIONER LEMAN: Are there cases where
9 you have to make arrangements or where you do make
10 arrangements with the securities commissions about
11 who is going to take action in a certain case? Is
12 there an area there where it is not quite certain
13 whether they should take action or you?

14 MR. BEATTY: In all the recent cases I
15 am aware of the securities commission have been
16 quite happy to have us look after the matter. They
17 prefer it that way.

18 MR. MILNER: There is a big, broad field,
19 Mr. Leman, that is not in any shape or form criminal,
20 if that is the right term to use, but is unethical.
21 For instance, we have had occasions where some of
22 our members have published what we deemed to be un-
23 ethical circulars. I do not think any court of law
24 could attack it but we feel that they are not the
25 right way to be presented to the public and that is
26 the type of minor disciplinary action we can take
27 to be sure that those people do not use the mails
28 or the public advertisements to the detriment, we
29 believe, of our industry or to the detriment of
30 investors.



1 THE CHAIRMAN: I suppose the advantage
2 to members of the Association is that they become
3 known as members of an association which is governing
4 itself and imposing certain standards upon its members
5 and what amounts to perhaps a code of ethics which
6 was perhaps agreed to and that that gives the whole
7 membership of the Association a prestige in the eyes
8 of the public and people prefer to deal with people
9 who are members of an association of this kind rather
10 than a person who is not admitted for some reason?

11 MR. MILNER: That is exactly the purpose
12 we have in mind with our disciplinary actions, to
13 try to be sure that our image to the public is as
14 clear as it is possible to be.

15 MR. GASSARD: May I add, Mr. President,
16 one of the major functions of our president is to
17 carry this image abroad both to the members and to
18 the public. Mr. Beatty will be starting his presi-
19 dential travels early in September and he will have
20 a number of messages to carry to the members which
21 he addresses in a general group of employees and
22 then he meets separately with partners and directors
23 and every year I have seen our president carry some
24 new message, some new concept all of which adds up
25 to a continuing attempt to mold a growing and more
26 mature approach to our responsibilities and a standard
27 of ethics and standard of competence which keeps pace
28 with the growth of the industry.

29 THE CHAIRMAN: Do I understnad the securities
30 commissions encourage this? Do they think it is better



1 for this field of industry to be in the hands of the
2 members who are active in it other than being subject
3 to direct control by the state where everybody is on
4 his own and some of them trying to get away with
5 as much as they can?

6 MR. GASSARD: For some years now, Mr.
7 Porter, we have kept close liaison with the various
8 securities commissions and sometimes with the Attorneys
9 General pointing out to them the importance of uniform
10 legislation uniformly administered and I imagine that
11 that will be one of Mr. Beatty's major themes this fall
12 as he goes across the country. That keeps the
13 commissions informed of our opinions and there is a
14 sort of cross fertilization taking place that usually
15 results in benefits to both sides. We are not waiting
16 for the government to impose something on us: we
17 are discussing and imposing views on them periodically.

18 COMMISSIONER LEMAN: Your paragraph 56
19 on page 44 implied that there were still a few areas
20 where you were encountering trouble and that you felt
21 there should be some improvement. What are the
22 types of troubles you still run into and are not quite
23 satisfied with?

24 MR. MILNER: There are unquestionably a
25 lot of things we do not even know that have happened.
26 We only see the ones that are brought to our attention
27 in the main. But if you can go back to the image that
28 it is in our own best interest to attempt to improve
29 our own public relations and our public image to the
30 fullest extent to have it brought out, we think we can



1 do a better job by doing that than by having govern-
2 ments do it the other way around.

3 For instance, what we are doing now is
4 putting in a new by-law screening all our sales force
5 completely. Every person who is registered as a
6 salesman now with any one of our members or to be
7 registered will have to get the approval of the
8 local provincial committee before that salesman is
9 allowed to go out and sell securities to the public.
10 There will be a central registry between ourselves
11 and the stock exchanges on all salesmen so that people
12 who have got into trouble in, let us say, one of
13 the stock houses, let out for unethical reasons,
14 not necessarily criminal but unethical reasons, would
15 have a very difficult time in getting a license
16 in the Investment Dealers and vice versa.



1 It is all an attempt to upgrade the type of people
2 that are in contact with the public.

3 MR. BEATTY: It involves ethics and competence.

4 THE CHAIRMAN: But the Investment Dealers'
5 Association is recognized by this securities Act, is
6 it not? The Investment Dealers' Association appears
7 somewhere in the Act?

8 MR. GASSARD: In four provinces.

9 THE CHAIRMAN: It has certainly and undoubtedly
10 the blessing of the authorities to that extent.

11 MR. GASSARD: We hope it will be all the provinces
12 soon.

13 THE CHAIRMAN: Blessing is the right word.

14 COMMISSIONER LEMAN: You were talking of
15 practices now about which the regulatory bodies cannot
16 do anything, is that it?

17 MR. BEATTY: That is right.

18 COMMISSIONER LEMAN: They might know about
19 these things but because they are not criminal acts
20 they cannot do anything about them?

21 MR. BEATTY: Principally ethics and competence.

22 COMMISSIONER LEMAN: Now that brings us to
23 a question on which we have received various representations,
24 and that is the type of securities regulation we have;
25 statutory type. Primarily should there be a federal
26 body or should there not be one? You have expressed the
27 thought in paragraph 54 of Section E, and I think it
28 is Recommendation No. 30, that there be not constituted
29 in Canada what is called S.E.C type of legislation.
30 I do not think it would be worth anybody's time here to



1 start discussing any constitutional issue that might
2 be raised by that discussion, but we certainly can
3 look at the practical aspect of it nevertheless.
4 Constitutional issues can be solved by somebody other
5 than ourselves. Can you tell us briefly what are the
6 reasons you would be against an S.E.C. type of regulation?

7 MR. MILNER: I will ask Mr. Beatty to answer
8 that question.

9 MR. BEATTY: Disregarding the constitutional
10 problem which, incidentally, our council has grave
11 doubts as to whether the Federal Government has any
12 right in this regard, we have consulted the council
13 of Investment Bankers' Association in the United States
14 and our own council, and discussed the various areas
15 that are served by the Securities Act of 1933 and
16 the S.E.C. Act of 1934 in the United States. We could
17 find no area that we have not existing regulatory bodies
18 in Canada to serve what is looked after by these
19 organizations, so that in our opinion the establishment
20 of a federal body in Canada would be merely super-
21 imposing machinery on top of machinery that already
22 exists.

23 We do not feel that it would complicate to
24 a great extent the issuance of new securities, although
25 it would be another nuisance and another expense. We
26 feel that far more progress is being made and can be
27 made through the existing bodies working with them,
28 co-ordinating their activities, particularly the
29 provinces, and by examining and improving the administration
30 of the Companies Act.



1 Here we only have 10 provinces and the
2 Securities Acts in these provinces are consistent
3 and growing more consistent. Collaboration is excellent.

4 In the United States they have 50 States to
5 deal with, some of which had no securities regulations
6 whatsoever, so the problem was entirely different.
7 In the United States they found it was necessary to
8 form a national association of securities dealers
9 in order to properly administer and regulate the
10 operations of dealers of securities in the United States
11 in spite of the existence of the S.E.C. In other
12 words, the industry in the final analysis had to
13 police itself and does have to today.

14 COMMISSIONER LEMAN: Well, the S.E.C. is
15 not interested only in the industry as such, it is
16 interested also in the issuers and the standards they
17 must meet, so it is not just a question of the ethics
18 of the profession.

19 MR. BEATTY: That is right, but they had
20 some states with no regulations at all. We have no
21 provinces without regulations, and these regulations
22 are well administered and are becoming very similar
23 to each other.

24 COMMISSIONER MACKINTOSH: What you say, Mr.
25 Beatty, seems to be based on a confidence that our
26 provincial administrations could be brought to a
27 uniform degree of coverage and competence?

28 MR. BEATTY: Yes. There has been great
29 advances in the last year and they are all conscientiously
30 collaborating.



1 COMMISSIONER MacKEEN: While it might be
2 admitted that you could increase your sales, Mr. Beatty,
3 would a S.E.C. organization in Canada have more effect
4 on non-members?

5 MR. BEATTY: We do not think so, Mr. MacKeen.
6 We think the local bodies are far more competent than
7 a federal body would be. The operations that the
8 Securities Commissions desired to discourage require ---

9 COMMISSIONER MacKEEN: You have seen some
10 examples in recent years of certain gentlemen moving
11 from one province to another when they get caught up
12 by the provincial commission in their own provinces.
13 They move, for example, to Nova Scotia and New Brunswick
14 and continue to operate.

15 MR. BEATTY: Well, it is true but it is hard
16 to prevent a fellow from stealing if he is dishonest.
17 All you can do is catch him after he has done the
18 stealing. Not only do they move from one province to
19 another, they move from one country to another.

20 COMMISSIONER MacKEEN: Would a federal body
21 have more authority or catch up quicker with a man
22 say who gets in wrong in Ontario and moves to New
23 Brunswick? He operates there for quite a few months
24 before he is caught up with.

25 MR. BEATTY: That is possible.

26 COMMISSIONER MacKEEN: Especially if he does
27 not deal in that province of New Brunswick but deals
28 across the border.

29 MR. BEATTY: This is possible, but then he
30 will move to Lichtenstein or Panama and continue to



1 operate.

2 COMMISSIONER MACKINTOSH: Do you think we
3 have a favourable or unfavourable balance of trade?

4 COMMISSIONER LEMAN: Just to see where this
5 would lead us, we agreed that we would not deal with
6 constitutional issues, but let us just assume for a
7 moment that it would not be a superimposing agency
8 over the 10 agencies existing already. Let us just
9 assume that. We cannot prove it one way or another.
10 What would be your thought as to the value or cost
11 of getting a high standard of regulation and policing
12 in the whole country as one method against the other?

13 MR. BEATTY: As I say, we covered this with
14 the Investment Bankers' officials in some detail and
15 we really could not see any advantage that they had
16 over us as conditions exist today.

17 COMMISSIONER LEMAN: Well, now, let us look
18 at the various fields where this applies. There is
19 policing of the actions of the people of the profession,
20 and there is policing of the actions of the issuers
21 and, lastly, there are all the side issues like
22 supervision over stock exchanges and stock trading,
23 and that sort of thing. Let us take these one by one.
24 If we look at the issuers, it is mainly a matter of
25 the way prospectuses are used to sell securities. Is
26 it your feeling that there is nothing to say in favour
27 of our type of prospectus under the existing securities
28 legislation which we have in Canada as against that
29 in the United States?

30 MR. BEATTY: They have one advantage over us



1 in that they are able to issue preliminary prospectuses
2 in advance of the actual approval of the issue, and
3 thus inform potential buyers of the qualities of the
4 security which they are offering. On the other hand
5 they have quite a few disadvantages, particularly
6 in respect to the tremendous volume of material that
7 is required. It actually defeats itself.

8 The S.E.C. only requires full disclosure,
9 it does not regulate the quality of the offering.
10 All it does is require you to disclose any shortcoming
11 that there might be in the security, and by its very
12 volume it defeats its own purpose. A full prospectus
13 under the S.E.C. is such a voluminous affair that
14 very few people plough through it. Consequently a
15 disclosure in actual practice to the potential investor
16 is not as full as ours, where our processes are simpler,
17 consequently the volume of material is not as large.

18 COMMISSIONER LEMAN: Well, is it quite easy
19 for the legislator to sit down and foresee every possible
20 type of issue and say: You will have made full disclosure
21 if you answer questions A to Z? Do you feel that that
22 is a good full disclosure regulation?

23 MR. BEATTY: I think it is impossible.

24 COMMISSIONER LEMAN: Well then how do you
25 overcome that in Canada?

26 MR. BEATTY: I do not think you can overcome
27 it anywhere.

28 COMMISSIONER LEMAN: Well, is most of our
29 security regulation and legislation now based also on
30 the full disclosure principle?



1 MR. BEATTY: It is based on the whole disclosure
2 principle. I believe the disclosure that is required
3 now is adequate for any reasonable investment purpose.

4 COMMISSIONER LEMAN: Well, now, if this
5 is full disclosure in the United States and in Canada,
6 why does it take thousands of more words to make a
7 full disclosure in the United States than in Canada?

8 MR. BEATTY: I think it is Parkinson's law.

9 THE CHAIRMAN: In the United States do they
10 not itemize certain types of information that they
11 want and include a series of questions that have to
12 be answered?

13 MR. BEATTY: We have certain statutory
14 information which our legislators deem to be necessary.

15 THE CHAIRMAN: They seem to have more and
16 more.

17 MR. BEATTY: Yes, and more and more people
18 process it.

19 COMMISSIONER BROWN: Is it possible that by
20 having different authorities in Canada you get a
21 certain amount of competition? Let us use Ontario,
22 for example. If Ontario gets too strict so that it is
23 virtually impossible for an issue to be made in Ontario
24 they will be made in other provinces?

25 MR. BEATTY: It is possible.

26 COMMISSIONER BROWN: And this keeps things
27 down to a reasonable level. If you ever get one
28 authority will there be this danger of Parkinson's
29 law developing; that is no one to criticize it or
30 no others to compare it with, and it might get out of



1 hand?

2 MR. BEATTY: This is the point I am trying
3 to make. It would grow and grow. I do not believe
4 if we had a federal body that the provincial bodies
5 would disappear.

6 THE CHAIRMAN: The history of securities
7 regulations in Canada goes back to about the time of
8 the great depression, I think, and it was somewhere
9 around that time that there were a number of incidences
10 that occurred resulting in securities commissions being
11 set up, and since then they have gone through many
12 other phases of approach to the whole subject. At
13 first, as I recall it, they attempted to regulate
14 in some detail as to what should be disclosed and what
15 should not be disclosed, and what sort of spread should
16 be allowed, and various other matters of that kind,
17 and by experience over the years the viewpoint has
18 changed materially until now it is largely a question
19 of full disclosure. That is, reasonable disclosure
20 without being tied down to specific details, depending
21 upon the circumstances of the case. Is that not about
22 it?

23 MR. BEATTY: That is right.

24 THE CHAIRMAN: There has also developed a
25 considerable experience in regard to the enforcement
26 of the statutes.

27 MR. BEATTY: It puts any regulatory body
28 in an impossible position if they are asked to judge
29 the quality of a security. For instance, mining stock;
30 nobody can see what is under the ground. The Ontario



1 government for a while employed a geologist for the
2 Securities Commission to try and upgrade the quality
3 of the mining issues they were asked to approve, but
4 it would be absolutely impossible for 100 geologists
5 to visit every property that was registered, and even
6 visiting them, to know whether there was anything under
7 the ground or not.

8 COMMISSIONER LEMAN: The S.E.C. does not
9 employ geologists, does it?

10 MR. BEATTY: No, but it demands more and more
11 information of a technical sort such as is furnished
12 by geologists, which disclosed no more than the
13 Ontario geologists could disclose, but still must be
14 part of the prospectus.

15 COMMISSIONER LEMAN: Let us not get carried
16 away too much by the fact that people think that because
17 the United States dollar is called a dollar and the
18 Canadian dollar is called a dollar they should be
19 at par. A lot of people think that way. We say S.E.C.
20 type of legislation. We do not have to copy everything
21 they have done or use exactly the standards they have
22 used. We do not need to copy their regulations, we
23 can just dovetail them to Canada's needs. I fail to
24 see why you imply that Parkinson's law would operate
25 more on a federal level than it does at the provincial
26 level.

27 MR. BEATTY: One reason I have this view is
28 that I do not believe the provinces would disband their
29 securities commissions.

30 COMMISSIONER LEMAN: Well, we have assumed that.



1 MR. BEATTY: We are assuming that they
2 are disbanded?

3 COMMISSIONER LEMAN: Yes.

4 MR. BEATTY: This would be ideal.

5 MR. MILNER: That is ideal.

6 THE CHAIRMAN: If you do not have any at
7 all?

8 COMMISSIONER LEMAN: Am I to understand rightly
9 that your opinion then is based on the fact that this
10 be a superimposition over what exists, but it could be
11 assumed that either through legislation and through
12 agreements between the provinces and the federal
13 government there would be one single agency, then you
14 change your opinion?

15 MR. BEATTY: It would be perfect.

16 COMMISSIONER LEMAN: You think it might be
17 more efficient to have one regulatory body?

18 MR. BEATTY: I would like to go back to the
19 original discussion that we had which led us to believe
20 that our system is very good now in comparison with
21 that in effect in the United States.

22 COMMISSIONER BROWN: I would like to explore
23 this question a little bit further. You criticize
24 a possible S.E.C. type in Canada because of the
25 possibility of the development of, to use an expression,
26 Parkinson's law?

27 MR. BEATTY: That is right.

28 COMMISSIONER BROWN: If all provincial juris-
29 dictions disappeared and were replaced by one federal
30 jurisdiction ---



1 MR. BEATTY: This would be an improvement.

2 COMMISSIONER BROWN: You would not be afraid
3 of Parkinson's law taking place then?

4 MR. MILNER: No, but Parkinson's law would
5 apply at least in our opinion if we had a dual one
6 to go through. It would be simply adding a further
7 expense to all issuers. The cost of registration in
8 the United States is fantastically high.

9 COMMISSIONER BROWN: But they do not have a
10 dual situation?

11 MR. BEATTY: Yes, they do.

12 MR. MILNER: I am speaking of the cost of
13 the operation, I am not speaking of the cost of
14 registrations. The cost in Canada would be similarly
15 high in our view if we had to go through both a federal
16 securities commission plus a provincial securities
17 commission. What I understood Mr. Leman to say is
18 that he is arguing on the basis that there would be
19 only one securities commission.

20 MR. BEATTY: This would be ideal.

21 COMMISSIONER BROWN: This changes your
22 whole idea?

23 MR. MILNER: It alters our viewpoint completely
24 if you are talking about only one securities commission.

25 MR. BEATTY: In the United States they do
26 have state bodies as well as the federal one.

27 MR. SHAW: I think this is one area in which
28 we might find one wide amenity within our acts. I am
29 afraid that I cannot add here to the complete approval
30 of a body. I am speaking entirely personally, if I



1 might say so and qualify what I say to that extent.

2 It would seem to me that one of the advantages
3 of our present system is that the work to clear an
4 issue is now divided among the varying jurisdictions.
5 Even with that, because so many of the issues originate
6 in Ontario and Quebec, one of our difficulties is getting
7 clearances for issues in time to keep in tune with
8 the market that then exists. I think the Ontario
9 and Quebec Securities Commissions do an admirable job
10 as it is, but I would hesitate to say without qualification
11 that if all issues had to go through one agency, no
12 matter where they originated in Canada, that we could
13 expedite our issues and get them ready for the market
14 as quickly as it is important for us to do, as we can
15 do where the work is delegated and spread out through
16 the provinces.

17 To that extent I think I would have to express
18 some doubt that the one regulatory body in place of
19 what we now have would meet with complete approval.

20 MR. BEATTY: You would be nervous that
21 there would be an increased delay?

22 MR. SHAW: I would, indeed, and the delay
23 factor could well introduce an expense factor which
24 might be very important.



1 MR. MILNER: Could I ask if you would like
2 to speak to that?

3 MR. SUTTON: Well, I am speaking directly
4 on behalf of our own firm, and we would be in favour
5 of one regulatory body; as Mr. Shaw says, there is
6 this danger of delay, but it does take longer to
7 get clearance on the S.C.C. in the United States than
8 it does for us to get clearance here in Canada.
9 Nevertheless, it is conceivable that you might run
10 in to differences of opinion between different
11 provincial regulatory bodies. This has not happened
12 so far but it is something that we might be concerned
13 about for the future. Our own feeling is that if
14 we had one body it would be better, we would not want
15 another body superintending them.

16 COMMISSIONER LEMAN: Might I ask one of
17 the other large underwriting houses to speak on this?

18 MR. MILNER: Perhaps Mr. Strathy could
19 speak to that.

20 MR. STRATHY: Mr. Leman, for the past few
21 years when I was the chairman of the Toronto stock
22 exchange I had a lot of dealings with the Ontario
23 Securities Commission at that time and furthermore
24 I attended a number of the conventions or conferences
25 of the National Security administrators; they have
26 an organization themselves, the various provincial
27 security administrators and they meet once a year
28 or more often, and they discuss these problems that
29 arise between the various provinces and I have met
30 with a great improvement in arriving at a similarity of



1 legislation or control of the various security dealers
2 that come under their respective responsibilities.
3 This is a thing which perhaps has not been established
4 for many years because I believe that most of this
5 is a post war thing, that there has been a gradual
6 growing together of the work of the various provincial
7 securities administrators to the benefit of the whole
8 industry and to enable better understanding to prevail
9 between the various groups that deal in securities
10 and the various administrative bodies that control
11 it from the provincial point of view.

12 COMMISSIONER MacKEEN: That all leads up
13 to more uniformity?

14 MR. STRATHY: Yes. The requirement for
15 a national securities administration. I am convinced
16 that otherwise it would result in the development of
17 Parkinson's law and the increased time to get the
18 issue cleared and with the expenses that that would
19 entail and the fact that certain areas might never
20 come to market at all because the market conditions
21 had changed in the interim. It is practical and
22 it is becoming more practical and I have great hopes
23 that this will be achieved in greater measure as the
24 years go by.

25 THE CHAIRMAN: You visualize a central
26 body sitting in Ottawa, no doubt, to which everybody
27 would have to come to have their issues dealt with.

28 MR. STRATHY: No, I do not visualize that.

29 THE CHAIRMAN: When you say it takes more
30 time that would be because it would be centralized?



1 MR. STRATHY: Everything would be funnelled
2 through a central body; there would hardly be enough
3 personnel to handle all the problems in all the new
4 issues they are faced with, not only issues from the
5 Investment Dealers' Association but they are a very
6 broad ramification of the whole matter of new security
7 issues in Canada; any mining stocks, and what have you.

8 Each province has problems but not quite
9 similar with the other provinces, so that that
10 particular province knows its particular problems
11 much better and knows how to handle them than, say,
12 another province. In Ottawa they would have to
13 handle the whole broad scope of the industry, which
14 is much wider than we are talking about here, the
15 investment dealers.

16 COMMISSIONER LEMAN: There is the question
17 of stating what the requirements are and also the
18 matter of enforcing them, and in the area of enforcement
19 it might be more frequent. However, let us pass on
20 to the other aspect.

21 We talked about a problem in relation to
22 acquiring issues and the matter of policing the
23 industry itself and you expressed a clear preference
24 for doing it yourself, and that can be understood, but
25 there is the matter of stock trading. The S.C.C.,
26 as I understand it, has jurisdiction over stock exchanges
27 too. Who has jurisdiction over stock exchanges in
28 Canada?

29 MR. MILNER: The various provincial securities
30 commissions.



1 COMMISSIONER LEMAN: I would think they do
2 not in relation to the standards of performance of
3 our stock exchange.

4 MR. BEATTY: They have used the self policing
5 method.

6 COMMISSIONER LEMAN: How would the two
7 standards compare, would you say, between the large
8 national exchanges in the States and ours in Canada.

9 MR. BEATTY: They both seem to have had their
10 difficulties. I would say that we have been just as
11 effective as they have. The problem arises, again,
12 in the technical nature of the business.

13 Where a case has come to court arising
14 from irregular dealings through a stock exchange it
15 has always proven extremely difficult to get a
16 conviction. They have never, for instance, convicted^{anyone}
17 of a washed sale, which is contrary to the law of the
18 land, but the industry in policing itself understands
19 these matters where a jury would not, and it is possible
20 to deal with it. Consequently your ultimate standard
21 is going to be higher through using the self policing
22 method than it is through using the legislative procedure.

23 COMMISSIONER LEMAN: Let us look at some of
24 the problems where weaknesses appear to exist from your
25 own suggestions here and let us take the point which
26 you raise in paragraph 58 of Section E. You are
27 referring there to a process called the "take-overs".
28 Now, you suggest that this Commission should take
29 an interest in this matter to see if shareholders
30 could be better protected. What do you have in mind



1 specifically in suggesting that?

2 MR. MILNER: I will ask Mr. Shaw to speak
3 to that.

4 MR. SHAW: Mr. Commissioner, this is, of
5 course, a matter that has been very much in the public
6 eye not only in Canada, but it is a matter of concern
7 in Great Britain, and has been dealt with in the
8 recent reports.

9 The objections to the take-over operations,
10 the so-called take-over bids that have occurred in
11 the recent few months have been related to basically
12 three factors. One, that the buyer has not disclosed
13 himself. The board of directors of the company
14 involved is in no position to advise the shareholders
15 as to the competence or desirability from the share-
16 holders' point of view of the new ownership or there
17 has not been disclosure of the prospective buyer.
18 There has been a limit on the amount of shares that
19 the prospective buyer has indicated a willingness to
20 buy and an indication of some haste, if you wish,
21 or desire to get the thing wrapped up and out of the
22 way quickly, so these bids have had the qualification
23 that they will leave the offer open until a given date
24 or until a given number of shares have been presented
25 at the price offered.

26 The objection there is that if the offer
27 would appear to be so attractive that the shareholders
28 want to rush in and deposit their shares immediately,
29 that those who are nearby get theirs in first, and
30 those who are some distance away or for one reason or



1 another are unable to get them deposited, are out, so
2 that brings up the third difficulty that the offer is
3 not open long enough.

4
5 A suggested manner of dealing with this
6 is one which would deal with each of these things
7 separately; first of all there should be a full dis-
8 closure of the prospective buyer; if there are more
9 shares deposited than the buyer is willing to buy,
10 that the offer then should be made operative on a
11 proportionate basis, and if there are 100,000 shares
12 wanted and 200,000 shares presented, or 200,000
13 shares outstanding, that 50 per cent of those present
14 holdings would be taken over. Also, in any event,
15 that the thing should be left open for a sufficient
16 length of time to permit people under normal cir-
17 cumstances to get to their boxes and the services
18 to be physically applied.

19 COMMISSIONER LEMAN: That all sounds
20 quite reasonable, Mr. Shaw, but who should impose
21 this code of procedure?

22 MR. SHAW: Let me say that these are the
23 suggestions that are put forward, and there is some
24 question as to whether everyone involved or everyone
25 within our industry would say that these suggestions
26 in themselves are sufficient.

27 First of all for the reasons you suggest,
28 who would impose the policing, and if they are
29 listed shares, the inference seems to be that the
30 stock exchange would say that if it is a listed share



1 that that is what must be done or the listing privileges
2 would be jeopardized.

3 It was suggested that there may be other
4 circumstances which should be taken into account. What
5 happens, for instance, in the event of a large holding
6 company, if you wish, becoming interested in a company
7 and watching its progress over a period of months or
8 even years and gradually accumulating these shares and
9 saying that here is a situation which we may want to
10 be in a major holding position. They end up, if they
11 are seeking operative control, they wind up at some
12 stage where they need X number of shares -- it may
13 be 50,000 shares or it may be more or less -- and at
14 that stage they then say, "Well, we are going to wrap
15 this thing up; we want 35 per cent or 51 per cent" --
16 or whatever percentage they feel they need and they
17 go over the shareholders' list and they pick on eight
18 or ten large shareholders and they go to them and they
19 say that they will make a bid for all of their non-
20 par shares at a price which must be made attractive
21 to attract their attention, and they go to only those
22 six or eight shareholders. What happens is that ---

23 COMMISSIONER LEMAN: I do not want to
24 interrupt you, but our time is passing by and my point
25 is this; I do not think we should go into the details
26 here as -- the details of what would be the right
27 procedure, but the thing is who should decide the way
28 it should be done, which is the proper, fair and honest
29 way of doing it. Who should decide that and who should
30



1 impose it?

2 MR. SHAW: I am assuming that we -- I think
3 I am right in this; we have made no specific recommendations
4 in this respect.

5 COMMISSIONER LEMAN: But you feel that there
6 should be some kind of regulation for this sort of
7 process to take place?

8 MR. SHAW: I may have misunderstood your
9 question; I thought we were dealing with the reasons
10 why we feel we are in a position to make this
11 recommendation. I do not think that -- personally
12 I have not the answer.

13 COMMISSIONER LEMAN: But have you no idea
14 of what would be the proper agency to deal with a problem
15 of this kind?

16 MR. SHAW: The obvious ones, obviously,
17 would be -- if there are shares of stock -- the stock
18 exchange is involved.

19 COMMISSIONER BROWN: Would it logically be the
20 stock exchange, because if you did wish to have a
21 stock listed, this might be just what the would be
22 take-overer wants.

23 MR. SHAW: I would be glad to toss this
24 ball to somebody else.

25 MR. ELY: I have a view on that. I do not
26 think it is the stock exchange so much, and I have
27 not discussed it with anyone in our industry, but
28 there must be a way through the company or something
29 which makes it impossible for a non-disclosed buyer
30 to take over. In other words, it could be through



1 the Companies Act that no take-over bid can take place
2 unless the people taking over are disclosed. Once
3 that happens can the onus not be put on the company
4 to deal with that person on the basis of pro rata;
5 no take-over or take-over. How could it still be
6 if there are instructions to the contrary?

7 COMMISSIONER LEMAN: That is raising
8 another nice legal problem; the Companies Act does
9 not deal with the form of securities trading.

10 MR. ELY: I do not know what the reason
11 is.

12 COMMISSIONER LEMAN: What control does
13 the company have? Even the board of directors do
14 not know who these people are.

15 MR. SHAW: There was a recently publicized
16 incident where the security commissioners for Ontario
17 said flatly, "It is not within my province, it is
18 up to some other body" and inferred that it was the
19 stock exchange, and I believe it inferred it was
20 our responsibility. I think I am correct in saying
21 that up to the moment we do not know the answer in
22 the Association just where this responsibility should
23 lie.

24 COMMISSIONER LEMAN: Let us resort to our
25 big brother below the border; how is it handled down
26 there, who handles this sort of a problem?

27 MR. MILNER: In the United States they have
28 the same difficulty in small companies; they have no
29 difficulty with companies listed on the New York Stock
30



1 Exchange, their rules are adamant.

2 COMMISSIONER LEMAN: It is the stock
3 exchange rules?

4 MR. MILNER: Yes.

5 MR. COX: I think that only covers a
6 few of them, the major ones.

7 MR. BEATTY: It is a very difficult problem
8 and one which we have not ignored; we have discussed
9 it at great length, but the only recommendation which
10 we can come up with that we feel is constructive and
11 workable is this one of disclosure. The technicalities
12 which are in the best interests of the purchaser
13 and the vendor are so complex that it seems impossible
14 to work out a pro rata arrangement or a "first come
15 first served" arrangement that serves everything
16 that is being sought in a take-over.

17 COMMISSIONER BROWN: I suppose there could
18 be some penalty under the Companies Act if they
19 were dealing in their shares in that way?

20 THE CHAIRMAN: It is a matter of legis-
21 lation.

22 MR. BEATTY: An appropriate body,
23 yes.

24 COMMISSIONER MacKEEN: You can have many
25 of these Companies Acts to deal with.

26 MR. LEMAN: How about forbidding trustees
27 from acting?

28 MR. BEATTY: It could be by self policing
29 bodies.

30 COMMISSIONER BROWN: It is a Companies Act



1 problem and not the Securities Act.

2 MR. MILNER: In our recommendations and
3 suggestions this falls under this group where we say
4 we do not know the solution; it is a complete matter
5 of law as to whether it should be put into the Federal
6 statutes or the provincial statutes, but we are not
7 lawyers and we do not know what the answer is, but
8 we do say that here is something that there should
9 be definite steps taken to improve the present
10 situation, which is not a good situation for this
11 country or any other country, but quite frankly we
12 do not know how it should be approached and we are
13 putting it to the Commission, and saying that here
14 is something which we think must have your con-
15 sideration as to how it should be done; we leave
16 it to you to do that part of it. If you wanted
17 us to say we will appear back in October or November
18 and wanted us to consult with the legal profession,
19 that type of thing, you are on a different basis.

20 COMMISSIONER BROWN: In the same context,
21 whether
22 would you care to discuss this question of continuing
23 information about the corporation's affairs to their
24 shareholders. This again is a legal problem as to
25 who is to say that this must be done. This probably
26 falls more into the province of the stock exchange
27 and it also falls into the Investment Dealers'
28 Association with respect to companies that issue
29 debentures and bonds but whose common shares are not
30 held publicly and the only information given out
at the time of the new issue.



1 MR. MILNER: Well, the best example that you
2 could use for what might be called, I don't say "perfect"
3 but very workable legislation is , that the New York
4 Stock Exchange has not only full disclosure at the
5 time of an issue, but they force full disclosure in
6 perpetuity. There must be full disclosure of the
7 various facets of the company, but that only applies
8 to the one stock exchange. Here we have got three
9 main stock exchanges: Toronto, Montreal and Vancouver,
10 and we also have nine provincial securities commissions,
11 and it seemed to us there must be some way of tying
12 in the securities commissions plus the stock exchanges
13 to having perpetual full disclosure. I think, as
14 Mr. Brown quite rightly says, you run into it on a
15 bond issue of a company that has no common shares,
16 and a person does not know until the day he dies what
17 the company has done.

18 COMMISSIONER BROWN: Could the underwriter
19 have an agreement with the trustee this information
20 will be supplied?

21 MR. BEATTY: This is frequently the case --
22 usually the case.

23 COMMISSIONER BROWN: This arises quite frequently
24 on debenture issues of subsidiary companies?

25 MR. MILNER: On the question of disclosure,
26 it is very hard to force people to disclose
27 who don't want to disclose. You may quite rightly
28 say, "Don't underwrite an issue" -- that would be
29 your answer. If the people are not willing to disclose,
30 you should not sell the security, but unfortunately some-



1 one always will sell a security if you don't -- if
2 it is a good security. I think you have got a perfect
3 example in the T. Eaton Company. There is a company
4 every person believes is a very well run industrial
5 company, but no one knows if it is or not. No one
6 has ever seen their balance sheet.

7 THE CHAIRMAN: They don't publish their
8 statements -- just the way you don't.

9 COMMISSIONER LEMAN: Everybody thinks most
10 of you are well run, but nobody knows either.

11 Well, the Security Analysts Society in
12 Toronto made that same request, that the commission consider
13 this matter of disclosure and good standards of financial
14 statement publication etc., and we didn't get to any
15 conclusion with them. We asked them if the Investment
16 Dealers as a group could obtain this of companies
17 before they agreed to handle their securities and they
18 said, "Perhaps if there could be unanimity among
19 the group we probably could, and with the co-operation
20 of the stock exchanges we probably could obtain it",
21 but they didn't seem to think the association was
22 quite ready to take the necessary steps to obtain it.
23 That led us into asking them, if the private sector
24 won't do it, perhaps an S.E.C. type of legislation would
25 do it, and they were not in favour of that. So, we
26 are just trying to get a little help from you as to
27 which are the best ways of obtaining these things
28 which everybody seems to think are desirable.

29 MR. STRATHY: Surely, it must be through
30 forces of legislation in the final analysis, and it



1 applies to all companies whether they are companies
2 that are financed through the I.D.A. or stock exchanges
3 or any other organizations. It surely applies to
4 all public companies. Therefore, public companies
5 are either with provincial charters or federal charters,
6 so it has to be a federal enactment and a provincial
7 enactment.

8 COMMISSIONER LEMAN: Well, let us go on to
9 the next problem concerned with this whole area, which
10 is your recommendation -- you seem to have some
11 misgivings about some trends related to mutual funds.
12 Recommendation 31, for instance, suggests that perhaps
13 there is need for regulation of mutual funds. What
14 are the problems there? What do you have in mind?

15 MR. FOWLER: To some extent I speak for myself
16 because it is not a subject which has been discussed
17 too much amongst the members, but basically I feel
18 that regulatory legislation should be introduced.
19 Presumably it would have to be at provincial levels
20 under the present setup, which pertains to the mutual
21 funds themselves.

22 The first thing is that legislation should be
23 at least uniform in its concept and administration in
24 all provinces. At the present time as far as the
25 mutual funds are concerned, as far as I know, there
26 are no actual regulations pertaining to investments.
27 I think a great deal has got to be said about all the
28 major funds, that they have entirely voluntarily set
29 their own standards which are very high, and they rather
30 conform with the standards which the S.E.C. lays down



1 for mutual funds in the States.

2 There should be legislation on limitation of
3 investments; that is, mutual funds should not be
4 allowed to own, we will say, a controlling interest
5 in any particular company if it is going to function
6 in a true sense as a mutual fund.

7 There should be restriction against practices
8 such as selling short or buying on margin which are,
9 again, contrary, to my mind, to the public trust, shall
10 we say, in mutual funds.

11 There should be also legislation which ensures
12 arms length dealing and which would avoid any conflict
13 of interest between management and the shareholders.

14 There should also be a maintenance of appropriate
15 and uniform standards of advertising and sales literature.
16 There is a great spread on that at the present time.
17 I think again we have got to say the major mutual funds
18 have done an excellent job, but there are some smaller
19 ones where, to my mind, a lot of their literature
20 could be misinterpreted if you were not a reasonably
21 sophisticated investor.

22 The other one is that I think all mutual
23 funds should be required to have a clear statement
24 of the policy of the company. This is to prevent mutual
25 funds from using the name "mutual fund" as a cloak to
26 carry on other perfectly legitimate investment business.

27 I think those, Mr. Chairman, cover the main
28 points that I have in mind. The thing is at the
29 present time there is no legislation that I know of
30 pertaining particularly to mutual funds. There is one



1 that comes under the Income Tax Act, in Section 69,
2 whereby a company cannot derive more than 10 per cent
3 of its income from one corporation. That is about the
4 only regulation there is in existence, as far as I know.

5 COMMISSIONER LEMAN: But mutual funds are
6 sold in Canada partly through members of the Association
7 and partly outside the members?

8 MR. FOWLER: More funds are selected by --
9 they usually call it the underwriters of the actual
10 mutual fund; the "sponsors" may be a better word.
11 There are more shares of mutual funds sold by them than
12 by the Investment Dealers.

13 COMMISSIONER LEMAN: Their salesmen, when they
14 sell direct, have to be licensed salesmen?

15 MR. FOWLER: They have to be a licensed
16 salesman, but as far as I know there is no specific
17 standard that the salesman has to attain. Frankly, I
18 think I am walking into ground that is away from the
19 investment dealer and into their field a little when
20 I make that statement, but I do know of many instances
21 where the man has had maybe two or three days training
22 with the sales organization and then he is out selling
23 mutual shares.

24 COMMISSIONER LEMAN: If they are licensed
25 salesmen, this whole realm of regulation you are talking
26 about would come under the jurisdiction of the provincial
27 securities act, wouldn't it?

28 MR. FOWLER: Yes sir, as far as being a salesman
29 is concerned, but as far as the fund itself is concerned
30 there are no regulations. They have to comply with the



1 various provincial regulations in regard to the issue
2 of a prospectus. They have to provide the necessary
3 statutory prospectus and that sort of thing, but there
4 is no regulation I know of either on a federal level
5 or provincial level which specifies in the manner that
6 is dictated by the S.E.C. as to the mutual funds
7 investments -- that they cannot purchase more than a
8 certain percentage of a certain company or that they
9 cannot sell short.

10 I would like again to emphasize the fund
11 themselves on a purely voluntary basis, I think, have
12 been very, very careful in setting up a very high
13 standard, but that does not mean that without the
14 necessary regulation it will continue.

15 COMMISSIONER GIBSON: Would you restrict the
16 investment powers to any further degree? You said:
17 Not more than 10 per cent; make sure transactions are
18 at arms length; no selling short or buying on margin?

19 MR. FOWLER: I haven't really worked out any
20 particular thing, but I definitely would be against
21 buying on margin, selling short and things of that
22 nature.

23 COMMISSIONER GIBSON: How about the kind of
24 asset they are allowed to purchase? Any restrictions
25 on that?

26 MR. FOWLER: No, I don't think we should do
27 that because providing the fund reveals -- and again,
28 they publish quarterly reports of the securities they
29 hold, and the owner of the shares knows very regularly
30 what has happened, and that is one of the advantages,



1 at least one of the things why the public have gone
2 for the mutual fund in the way they have, that they
3 like the attitude of the management operating in a
4 goldfish bowl at all times.

5 COMMISSIONER LEMAN: You are looking to the
6 future mostly in your recommendation? You are not
7 too worried about the present situation?

8 MR. FOWLER: No, I think at present we have
9 got to give the fund very high marks.

10 COMMISSIONER LEMAN: Lastly, and still in this
11 general area, there is a question I would like to ask
12 you: What, in your view, should be the relationship
13 between stocks exchanges in a country? Is there an
14 area where they can compete, and what is that area?

15 MR. MILNER: I am sorry I didn't quite get
16 your question.

17 COMMISSIONER LEMAN: What generally should be
18 the relationship between stock exchanges in a country?
19 Are there areas where they can compete and where
20 it is useful that they compete, and what are these
21 areas?

22 MR. CRETZIANU: Well, I would not speak of
23 competition between stock exchanges, but I certainly
24 think that the arbitrage transactions which can be done
25 between the markets can help in the better pricing
26 and distribution of securities. Certainly, the fact
27 also that a stock exchange such as, say, San Francisco
28 is able to operate for two or three hours later than
29 the New York Stock Exchange is also helpful to the
30 better distribution and pricing of securities.



1 COMMISSIONER MACKINTOSH: Are there any
2 limitations on arbitrage operations among Canadian
3 exchanges?

4 MR. CRETZIANU: I am not too sure of that now.
5 I haven't followed it recently. There have been certain
6 changes.

7 MR. STRATHY: There is not really a great
8 deal of arbitrage, so-called arbitrage, taking place
9 in the securities listed on stock exchanges in Canada,
10 because in a great many cases you will find a member
11 of a stock exchange is a member of more than one
12 stock exchange. So, in part, that satisfies the
13 requirement of achieving the best market for the buyer
14 or the seller of the stock.

15 COMMISSIONER MACKINTOSH: He puts the order
16 in the exchange ---

17 MR. CRETZIANU: He puts the order on the
18 exchange where the best fill can be obtained, or, if
19 it is a bigger amount of shares he splits it amongst
20 various stock exchanges. There is arbitrage but it
21 has been, I would say, dying to quite an extent, but
22 it does have this effect in levelling the markets
23 between the various stock exchanges. In actual practice
24 the arbitrage is confined to industrial stocks between
25 Toronto and Montreal and very little more than that.
26 There is no arbitrage to speak of in minor stocks.

27 COMMISSIONER MACKINTOSH: You say it is dying:
28 You mean because there is not sufficient spread to make
29 a living on it?

30 MR. STRATHY: That is right and because the



1 stock exchanges have firms members of more than
2 one stock exchange.

3 COMMISSIONER MACKINTOSH: There is no restriction
4 on fishing, but there are no fish?

5 MR. STRATHY: There are less fish.

6 COMMISSIONER LEMAN: Would there be any
7 arguments in favour or against just having one stock
8 exchange with branches as against having numerous
9 stock exchanges?

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1 MR. STRATHY: Well, I would say that the
2 object of the stock exchange is to provide a marketplace
3 so in the United States in the main the prime stocks
4 are listed on the New York Stock Exchange. That does
5 not mean that certain of those stocks are not listed
6 on the midwest or Pacific coast exchanges but the prime
7 market is the New York Stock Exchange. Those that
8 do not achieve that prime degree of respectability or
9 what have you or record of earnings are listed on
10 the subsidiary stock exchange, the American stock
11 exchange. That does not apply so much in Canada
12 because in Canada there are really two major exchanges,
13 the Montreal and Toronto stock exchanges. There are
14 a great many similar listings on both exchanges. There
15 is the Vancouver stock exchange which might be deemed
16 a prime stock exchange but it is much smaller and on
17 that stock exchange also are listed many of the stocks
18 that are listed on the Toronto and Montreal.

19 Now, really a broader market could be
20 achieved if there was one stock exchange if you were not
21 looking at the other factors that come into the picture.
22 It might be said that you would achieve the best results
23 by having a number of stock exchanges each having different
24 listing qualifications so that the very large companies
25 with a long record of earnings and sound management
26 could be on the prime stock exchange like New York,
27 the secondary group might be on another stock exchange
28 like the American et cetera, but we have built up a
29 system which has more or less happened which is different
30 than the United States and it fulfills its function



1 reasonably well, I would say. But it only applies to
2 listed stocks and that is only a small proportion of
3 the public companies with shares in the hands of the
4 public.

5 THE CHAIRMAN: Adjourn for ten minutes.

6 (At this point a short recess was taken.)
7

8 THE CHAIRMAN: We shall now resume.

9 COMMISSIONER LEMAN: Mr. Milner, before
10 the recess I asked a question -- perhaps I did not
11 put it quite clearly but I did not get an answer to
12 it and the question was: Are there areas where
13 exchanges can compete with each other. There seemed
14 to be a reply that there was no such thing as
15 competition between stock exchanges. Is there any-
16 thing stock exchanges can do to encourage listing
17 on them and to encourage trading on their particular
18 exchange as against other exchanges, or is there no
19 such process of competition going on?

20 MR. MILNER: No, stock exchanges can
21 compete for listings to the detriment of the securities
22 to the extent that one stock exchange might waive
23 clause 3 (c) on the listing of proper disclosure
24 and if the company so desires or did not want to
25 give the information they might list on that stock
26 exchange and not have to give the information. It
27 would be far better if the stock exchanges had identical
28 restrictions as to listing.

29 COMMISSIONER LEMAN: So that any area in
30 which stock exchanges may compete with each other would



1 not produce any particular good to the securities
2 industry; on the contrary it would be the other way
3 around, is that right?

4 MR. MILNER: Well, the competition, I
5 think, is proper competition, the competition of
6 attempting to build up bigger businesses. Probably
7 more business would be done in two big stock exchanges
8 rather than one. That competition is good. Of
9 course, a national exchange would have the same
10 effect in the long run, but the fact is people want
11 to deal in their own stock exchanges, that is, the
12 people in Quebec all prefer to deal on the Montreal
13 stock exchange and the people in Ontario, I fancy,
14 are more anxious to deal on the stock exchange, on
15 the Toronto stock exchange, and if you go out west
16 you have the same thing in Vancouver where your Vancouver
17 people prefer to deal on their own exchange.

18 COMMISSIONER BROWN: There is one factor
19 that does affect this and on which I think we would
20 like to have some comments and that is provincial
21 transfer taxes.

22 MR. MILNER: Well, of course, we are against
23 provincial transfer taxes.

24 COMMISSIONER BROWN: That is the answer I
25 expected.

26 THE CHAIRMAN: I have heard this for many
27 years.

28 COMMISSIONER BROWN: But it does affect
29 the mobility of capital in Canada?
30



1 MR. MILNER: It affects the mobility of
2 capital in Canada and also the succession duties have
3 the same effect. That is the reason that you get
4 so many transfer agents. Some of the larger companies
5 have transfer agents in three or four provinces merely
6 to get around that.

7 COMMISSIONER BROWN: Some of the largest
8 ones have not?

9 MR. MILNER: No, some of them have not.

10 COMMISSIONER LEMAN: Well, the stock
11 exchanges will come before us and they will be able
12 to defend themselves, Mr. Milner. We wanted your
13 opinion on some of these points. That is all I
14 have in that area.

15 MR. MILNER: Mr. Leman, you asked one
16 question before lunch and I said we would endeavour
17 to answer it this afternoon. I am going to ask Mr.
18 Cretzianu to answer it.

19 MR. CRETZIANU: I have made a quick
20 estimate of these pooled funds and I find that life
21 insurance companies in Canada at the end of 1959
22 had assets of \$7,500,000,000 while in the United
23 States their assets were \$125 billion. So it is
24 quite clear, if you want to take the population
25 ratio, that these funds are much higher in the States.

26 Trustee pension funds, I made an estimate
27 of around \$3 billion against \$33 billion so there
28 it would be a little closer.

29 Investment funds -- in 1960 in Canada
30 were nearly \$750 million net worth of assets and in



1 the United States they were \$20 billion, so there
2 again it is quite clear that the proportion in the
3 United States is much higher.

4 MR. MILNER: Does that answer your question,
5 Mr. Leman?

6 COMMISSIONER LEMAN: Yes it does, thank
7 you.

8 COMMISSIONER MACKINTOSH: Mr. Chairman,
9 I have a few questions I would like to ask in clarification
10 of some parts of the submission. In Appendix D on
11 municipal finances in paragraphs 12 to 15 there is
12 an explanation of the need to have some systematic
13 municipal statistics. Has the Association asked
14 for these statistics from the various departments
15 of municipal affairs and been unable to obtain them?

16 MR. MILNER: Mr. Johnson, would you care
17 to speak on that?

18 MR. JOHNSON: I know of two instances where
19 the provincial governments have been asked to improve
20 on the information that has been provided. We are
21 provided with some information. It is usually late
22 in reaching us. The main complaint in one province
23 is that you get the information the day of the tender
24 or the day after whereas we require it about two weeks
25 in advance. The information that is provided in this
26 instance is quite complete.

27 COMMISSIONER MACKINTOSH: Would it be
28 impossible to get the provinces, in the interests of
29 helping the municipalities with their financing, to
30



1 provide that they have to submit this information?
2 You have a form here of which part is statistical.
3 Why is not the sensible thing to have them submit
4 that when they ask for tenders? It was suggested
5 earlier that after a firm had got a tender that they
6 had to go back and ask the municipality what the
7 facts were about it. It seemed an awkward piece of
8 business. Why not have it required that if they
9 are going to put out bonds for tender they have to
10 supply the information?

11 MR. JOHNSON: Unfortunately the Association
12 cannot dictate the requirements, but the I think the
13 Association should put some pressure on various
14 provincial governments to provide the information
15 in good time. .

16 COMMISSIONER MACKINTOSH: Well, of course,
17 there is the extreme course of a member of the Association
18 not being able to tender. I know a lot of contractors
19 who will not tender unless the architect's specifications
20 and drawings are satisfactory. Part of that, I think
21 it is Exhibit A is, of course, qualitative and that
22 would have to be, I imagine, supplied by the dealer
23 himself if you are going to have a rating on the
24 facilities of the municipal council and the political
25 climate. I do not think that you can get any official
26 verdict on that.

27 MR. JOHNSON: No, we would not expect that,
28 sir.

29 COMMISSIONER MACKINTOSH: But with the rest
30 of the form I think it could be made a condition in



1 asking for tenders.

2 MR. MILNER: The difficulty, Dr. Mackintosh,
3 of course, in the small rural municipalities where
4 they have got inefficient local clerks of the council,
5 in the farm areas where a farmer acts as municipal
6 clerk and it is haying time and he does not answer
7 the inquiry. But there has been a vast improvement
8 in the municipal statistics over the last three years,
9 that is, the provinces in the municipal departments
10 have helped us considerably in getting statistical
11 information together. They have made it very awkward
12 for municipalities to get grants unless they submit
13 proper balance sheets and that is the quickest way
14 of getting the information.

15 COMMISSIONER MACKINTOSH: You have a
16 number of recommendations concerning municipal
17 securities. One which occurs somewhere in the body
18 of the submission is the suggestion of provincial
19 assistance in taking up issues and the various forms
20 which it might take. You suggest some grants might
21 be earmarked for the service of the debentures. Are
22 you referring there to special grants or to any grant
23 that is due to the municipality from the provincial
24 government?

25 MR. MILNER: Well, Mr. Johnson will say
26 what they do in Quebec there.

27 MR. JOHNSON: We refer there to special
28 grants and this is generally in the case of grants
29 made to school commissions where there is a grant for,
30 we will say, \$200,000 which is to be payable over a five-



1 year period at \$40,000 a year, and that grant is
2 specially earmarked for the servicing of the debt
3 during the years in which the grant is received.
4 Consequently, the first five maturities in the serial
5 issue are increased by the amount of the grant and
6 that enables us to sell those particular securities
7 at very close to the rate that would be received
8 on direct guarantee of the province, and, consequently,
9 the school commission not only benefits from the
10 receipt of the grant, but benefits from the slightly
11 improved cost of borrowing.

12 COMMISSIONER MACKINTOSH: This, in your
13 reckoning is a good thing?

14 MR. JOHNSON: Yes it is.

15 COMMISSIONER MACKINTOSH: What about the
16 practice in some provinces of using provincial funds
17 to purchase part of the issue which I gather helps
18 both the municipality and the underwriter?

19 MR. JOHNSON: That is very helpful but
20 it does not enable the borrower to obtain quite as
21 attractive a rate because the investor does not take
22 that into consideration when making his investment.
23 He is not buying something with a type of provincial
24 guarantee on it.

25 COMMISSIONER MACKINTOSH: He may not actually
26 know whether it is so or the degree to which it is so?

27 MR. JOHNSON: That is right, and as far
28 as the investors are concerned the security is no
29 better than if there was no agreement between the
30 government and the underwriters to purchase part of



1 the issues whereas if you have a grant the borrower
2 knows a certain part of the debt is going to be paid
3 off.

4 COMMISSIONER BROWN: If this is known before
5 the tender it encourages underwriters?

6 MR. JOHNSON: Where they might be concerned
7 about market conditions they are inclined to take a
8 little more risk than without that assistance.

9 COMMISSIONER BROWN: And would it not
10 at other times have the effect that if it was a very
11 competitive tender there is a tendency to work on a
12 narrower margin?

13 MR. JOHNSON: That is right.

14 COMMISSIONER MACKINTOSH: What about
15 provincial guarantees which I think you speak
16 approvingly of although you do not actually recommend
17 them?

18 MR. JOHNSON: We do not recommend them but
19 from the point of view of borrowing cost it does
20 definitely reduce the cost of borrowing to the
21 municipality but it also has the effect at times of
22 encouraging the municipalities to go out and spend
23 money more freely than they should.

24 COMMISSIONER MACKINTOSH: Yes, I do not
25 suppose any province is likely to offer an open
26 guarantee. They would keep some control.

27 MR. JOHNSON: We have seen instances where
28 issues have carried an unconditional guarantee of the
29 province and the money has just disappeared; it was
30



1 not properly administered.

2 COMMISSIONER MACKINTOSH: No province
3 extends beyond particular categories of municipalities?

4 MR. JOHNSON: It would be under very special
5 circumstances where the money probably could not
6 be raised otherwise in the volume required.

7 COMMISSIONER MACKINTOSH: What importance
8 do you attach to your recommendation that insurance
9 companies be allowed under the Insurance Act to carry
10 these securities at amortized book value?

11 MR. JOHNSON: I cannot give you a guess
12 at the percentage that the insurance companies might
13 increase their investment, but this is a problem
14 that we run into from time to time where insurance
15 companies have used that possibility as an out.

16 COMMISSIONER MACKINTOSH: As an argument
17 for not buying?

18 MR. JOHNSON: That is right.

19 COMMISSIONER BROWN: The insurance
20 companies came up with a similar recommendation but
21 it was not unanimous. It was the expression of opinion
22 of some that this prevented trading.

23 MR. JOHNSON: I think that some insurance
24 companies would increase their percentage investment
25 in municipals if they were permitted to amortize. This
26 has the effect of freezing them in certain instances.

27 COMMISSIONER BROWN: Could this be offset
28 by the inability it would place on the insurance companies
29 to place out municipal issues?

30 MR. JOHNSON: I would not be prepared to say



1 that it would offset it fully, but it would certainly
2 be of assistance in times of low market values where,
3 if they would be able to amortize, they would be closer
4 to the market level than they are at present.

5 COMMISSIONER BROWN: There is some argument
6 about restricting the amortization categories to those
7 that are obviously going to be met at maturity; in
8 other words, the obvious ones are Canadas where the
9 power of issuing the currency is in the hands of the
10 borrower and a slight extension of this would go into
11 the provinces, but how far are you extending this when
12 you get down to municipals?

13 MR. JOHNSON: I think it would be very
14 difficult to divide the municipalities up into those
15 where the securities should be amortized and those
16 where they should not be.

17 MR. MILNER: Well, Mr. Brown, the municipal
18 debt is probably in the last analysis the best debt
19 there is in the country if it is under proper control.
20 The willingness to pay of the small municipality is
21 unlimited. That is why we are loathe to have provincial
22 guarantees and that sort of thing to encourage a higher
23 ratio of debt than the municipality can properly carry.
24 But since the revision of the Municipal Acts after the
25 1929-31 period there have been practically no municipal
26 defaults, in fact I do not know of any municipal defaults
27 in the last ten years.

28 COMMISSIONER BROWN: One of the changes that
29 came about because of those problems was that I think
30



1 all municipal acts now require other than those municipi-
2 palities that are specially incorporated to issue only
3 serial or instalment bonds and not sinking fund. Would
4 you like to comment on this? Has this got an effect
5 on the present market?

6 MR.MILNER: I think I will ask Mr. Johnson
7 to answer that.

8 MR. JOHNSON: I do not think I got your
9 question.

10 COMMISSIONER BROWN: Do you think that the
11 market for municipal bonds would be improved or worsened
12 if municipalities were to go back to a sinking fund
13 type of issue rather than a serial type of issue?

14 MR. JOHNSON: You are talking about the
15 secondary market now or the primary market?

16 COMMISSIONER BROWN: Primary market.

17 MR. JOHNSON: I think the fact that there
18 would be some secondary market created by sinking fund
19 operations would improve distribution.

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1 COMMISSIONER MACKINTOSH: What is your view
2 of the suggestion we have had that they be allowed to
3 issue debentures which in the early years would be of
4 serials, and there would be a sinking fund for the
5 longer term?

6 MR. JOHNSON: That is the suggestion in this
7 brief.

8 COMMISSIONER MACKINTOSH: Oh, I see.

9 MR. JOHNSON: That is in this brief.

10 COMMISSIONER MACKINTOSH: I must have forgotten
11 what play we were producing.

12 MR. JOHNSON: You probably have two categories
13 of investors who buy municipals. You have short-term
14 buyers who like to buy one to five, or sometime one to
15 ten year serials, and your life companies and pension
16 funds have long-term investors who prefer a definite
17 one term, and we believe they prefer 15 or 20 years
18 sinking fund debentures rather than 11 to 15 years
19 serials.

20 COMMISSIONER BROWN: Would you like to see the
21 municipalities in Canada permitted to issue the type of
22 mortgage loans that the specific corporations in the
23 United Kingdom are permitted to issue?

24 MR. JOHNSTON: I am afraid I cannot answer that
25 because I do not know what they issue in England.

26 MR. MILNER: You mean redeemable ones?

27 COMMISSIONER BROWN: They issue redeemable
28 loans to individuals, and I think they are redeemable
29 in three months. If someone has £50,000 to put to work
30 they get in touch with their local corporation and arrange



1 to deposit it, and they get a piece of paper on which
2 they get the current interest rate which at the moment
3 is $6\frac{1}{2}$ per cent.

4 MR. JOHNSON: In other words it is short-term?

5 COMMISSIONER BROWN: Yes, redeemable on three
6 months notice, and they are fully registered.

7 MR. JOHNSON: I would not favour that.

8 COMMISSIONER BROWN: I did not think you would.

9 MR. JOHNSON: There is nothing selfish about it,
10 I was thinking of the municipalities.

11 COMMISSIONER BROWN: Do they get nothing out
12 of it?

13 THE CHAIRMAN: The initial debentures being
14 as good as you say they are, why is the differential
15 in interest rates so great?

16 MR. MILNER: Marketability is probably the
17 main factor, Your Honour. People who invest in
18 municipal debentures want a higher yield than they
19 do have in market debentures, whether it be one-quarter
20 of one per cent yield or one-half, I do not know. If
21 you are comparing Ontario as against a provincial issue,
22 a good municipal sells within one-quarter of one per cent
23 of the yield of the profits.

24 COMMISSIONER BROWN: Yes, but it is the type
25 of municipality that you described; the small
26 municipality which you put very high as being credit
27 worthy. Is it because the public do not realize that
28 it is as credit worthy as it really is? They are the
29 ones who can less afford to pay the high rate of
30 interest.



1 MR. MILNER: Not necessarily. I would not
2 think that would be a true statement. A small
3 municipality has just as good taxing power as the
4 large one.

5 COMMISSIONER BROWN: Yes, but it has not
6 got the big industry. They work on a much smaller
7 scale and do not spend the amounts of money that the
8 others do. They do not spend as much as the bigger
9 ones do, nor in the same proportion. Is it because
10 their credit worthiness has not been sold to the public?

11 COMMISSIONER MACKINTOSH: Mr. Milner, as you
12 said, first marketability and secondly, lack of knowledge
13 on the part of the investing public, is that true?

14 MR. MILNER: The lack of knowledge to some
15 degree, but actually it is the marketability which
16 accounts for the higher yield which attracts the
17 insurance company and the pension funds to buy municipal
18 bonds.

19 THE CHAIRMAN: Yes, but the marketability depends
20 to some extent upon the knowledge of the public as to
21 the value of the securities.

22 MR. MILNER: I would not think -- I do not
23 think that is nearly as much of a factor. If you start
24 dealing in the far northern securities where you are
25 dealing, for instance, in mining areas, there is
26 a risk element there.

27 THE CHAIRMAN: I am talking about the ones
28 that you say are first-rate. I assume that is what
29 you meant, that they are first-rate as far as credit
30 risk is concerned yet they are about third-rate in line



1 with interest rates.

2 MR. MILNER: There again you have got a somewhat
3 similar situation as was brought up this morning in
4 respect to provincial issues. Your provincial issues
5 do not sell in the same level of price. Buyers dictate
6 the price, we cannot dictate it.

7 THE CHAIRMAN: I understand that.

8 COMMISSIONER MACKINTOSH: If I can go back
9 to this question of amortized book values for these
10 municipal securities, I should like a little further
11 information in this regard.

12 Is it not a fact that for quite a number of
13 small municipal issues, a realistic market price cannot
14 be produced but can only be inferred?

15 MR. BEATTY: It is a great nuisance to investors
16 with large portfolios to have to value a large number
17 of individual items.

18 COMMISSIONER MACKINTOSH: May they not have
19 a debenture of small municipals with the most recent
20 sale that can be found being several months ago?

21 MR. BEATTY: They sit down and value them
22 all in collaboration with the dealers each year and
23 try to get a standard valuation for the use of the
24 insurance industry as a whole.

25 COMMISSIONER MACKINTOSH: Thus you only infer
26 values?

27 MR. BEATTY: You only infer values.

28 COMMISSIONER MACKINTOSH: If some other
29 security is selling for this, then this one ought to
30 sell for that?



1 MR. HUNTER: There is a market for all these
2 securities if these accounts want to sell them on the
3 secondary market. There is no active market for them
4 but they can put a price on their securities and the
5 dealers will go to work and sell them for them. There
6 is a reasonable amount of volume for that.

7 MR. JOHNSON: Dealers will buy them for
8 position also. There is no quoted market on them as
9 you have in Canada where you have a bid side and an offer
10 side. There is a bid side always and occasionally an
11 offer side if there are any bonds available.

12 COMMISSIONER GIBSON: This has the effect of
13 locking municipal security holdings and it is more
14 tightly into insurance companies portfolios. Would you
15 like to see that happen, or where is the trade in
16 municipal securities?

17 MR. JOHNSON: We would like to see more tradings
18 in them.

19 COMMISSIONER GIBSON: This is what is worrying
20 me. You want to allow insurance companies to value
21 these securities at the amortized book value, and yet
22 some of the insurance companies do not like this idea
23 because they would not feel like trading in them to
24 the same degree. There is a bit of a conflict here, I
25 think.

26 MR. MILNER: The trade, Mr. Gibson, in the
27 insurance companies in the secondary market on
28 municipals is not much at any time and, frankly, I do
29 not see what difference the amortized value would
30 have. In other words if a municipality two or three



1 years ago sold a security to yield 5 per cent to one
2 of the insurance companies, it is obvious that it will
3 take a wacking loss on today's market. Conversely, if
4 securities sold today to the insurance company from
5 a municipality, two or three years from now they could
6 easily dispose of this at a profit.

7 COMMISSIONER BROWN: Is this a guarantee?

8 MR. MILNER: Without guarantee.

9 COMMISSIONER BROWN: I mean, to sell them at
10 a profit? Can we quote you?

11 MR. HUNTER: I would like to point out again
12 that in 1961 primary sales of municipal securities were
13 approximately \$462 million, and yet there were \$368
14 millions of secondary market sales, so there is a market
15 for them.

16 COMMISSIONER BROWN: This is the point that
17 Mr. Gibson and I were making. Anything that tends to
18 look this market up is going to restrict this trading.

19 COMMISSIONER GIBSON: On the whole it is
20 definitely felt that if they carried them on their books
21 at the amortized value rather than the market or book,
22 whichever is the lower, they are much less likely to
23 sell them at a loss.

24 COMMISSIONER MACKINTOSH: If I can go back
25 to another recommendation, I should like to hear some
26 comment about it. I refer to Appendix B, provincial
27 financing, you recomend that the use of savings loans
28 type of issues be sharply curtailed.

29 MR. MILNER: Mr. Ely, would you like to speak
30 in that regard?



1 MR. ELY: I do not think it needs much comment.
2 I pointed out that savings loans are in effect a blank
3 cheque on the lender. Provinces do not control currency
4 and can find themselves in a very embarrassing situation.

5 COMMISSIONER MACKINTOSH: A blank cheque on
6 the borrower?

7 MR. ELY: I am sorry, a blank cheque on the
8 borrower, yes, if that borrower has not got control
9 of currency he is asking for trouble, and we have seen
10 some of it.

11 COMMISSIONER MACKINTOSH: Does the danger arise
12 from the existence of such loans or from the excessive
13 use of them?

14 MR. ELY: The excessive use.

15 COMMISSIONER MACKINTOSH: There is a small
16 stable market for that sort of thing in particular
17 localities, is there?

18 MR. ELY: The danger really arises, Dr.
19 Mackintosh, from excessive use, and they should be, I
20 think the words are used were, sharply curtailed. We
21 mean just that. They have been used far too excessively.
22 It is a means of raising money very easily, but a
23 very dangerous practice.

24 COMMISSIONER MACKINTOSH: Easy, but the
25 evidence is not clear that it is cheaply.

26 MR. ELY: The evidence is rather the other way.

27 COMMISSIONER MACKINTOSH: You have not any
28 rule-of-thumb as to how much is safe?

29 MR. ELY: None.

30 COMMISSIONER LEMAN: No rule, or no savings



1 bonds?

2 MR. ELY: No savings bonds by any other body
3 than the Dominion of Canada.

4 COMMISSIONER MACKINTOSH: Well, to turn to
5 another direction, and that is what you have to say
6 about chartered banks and near banks in Appendix H.

7 I am not entirely clear about your recommendation in
8 respect to the prompt adjustment of call loan rates to
9 fit market conditions. In the first place I gather
10 that the lag in adjustment causes you to borrow from
11 the street; I think you said country banks. Is this
12 in itself a bad thing?

13 MR. MILNER: Mr. Shaw, would you speak on that?

14 MR. SHAW: Well, this had the effect, Dr.
15 Mackintosh, that the so-called country bank market
16 expanded very rapidly and significantly in the period
17 from August 13, 1959, to September 29, 1960, when
18 contrary to the usual practice there was no difference
19 in the interest rate scale applied to dealer borrowings
20 from banks. The usual practice^{is} that there would be
21 interest rates scaled from the low to the most high
22 marketable securities, or short-term rather with the
23 lower rates scaled up to the high rates of long securities.
24 This is the longest period in our experience -- perhaps
25 not the longest period, but it so happened the rates
26 were set^{at} a flat $5\frac{3}{4}$ per cent at the initiation of that
27 period and were left unchanged for some 14 months.
28 This is a rate which would have made it extremely
29 difficult for us to carry on if this were our only source of
30 borrowed capital.



1 As a result the dealers were compelled to
2 look elsewhere, and I think we said with no little
3 success. This developed by reason of an apparent
4 indifference to the dealers' problems on the part
5 of the chartered banks. Their reasons probably were
6 very good.

7 COMMISSIONER MACKINTOSH: Maybe they were
8 elsewhere engaged.

9 MR. SHAW: They were perhaps elsewhere engaged;
10 at the same time the dealer found that there were other
11 sources of capital which grew to such large proportions
12 that we became alarmed as to the size of them and
13 started to measure that market. We put into effect
14 machinery for measuring it, which has remained since.

15 I think the recommendation states that if the
16 banks could share the dealers' ideas that the rates
17 would be periodically reviewed with a view to keeping
18 them competitive with other sources of borrowing loans,
19 the dealers in most cases would prefer to return
20 this trade to the chartered banks.

21 COMMISSIONER LEMAN: Is that because these
22 country banks are in and outers, or what?

23 MR. SHAW: No, it just imposed a good deal
24 more of a different procedure which was different to
25 what we have been accustomed. That is not to say
26 that now this market has been established it would
27 disappear entirely. There are many reasons why this
28 sort of thing has become of value both to dealer and
29 suppliers of capital.

30 COMMISSIONER MACKINTOSH: Would you not assume



1 that the banks are now aware of this historic experience?

2 MR. SHAW: We do so assume, and we had every
3 reason to believe that during the period that they
4 were aware of what was happening. However, as you suggest,
5 they were going through some problems of their own at
6 that time and had no difficulty in finding useful
7 employment for the funds that they then had.

8 Toward the end of the period we took occasion
9 to call upon one of the banks and discuss the matter
10 with them. They were quite aware of what was happening.
11 I do not suggest for a moment it was deliberate indifference.
12 It was simply that we had to seek capital on a basis
13 that would permit us to carry on business profitably.

14 COMMISSIONER MACKINTOSH: Well, what is uncertain
15 in my mind is whether this is simply the working or
16 the developing of a market under a set of strenuous
17 circumstances.

18 MR. SHAW: It was something that developed
19 under this impetus that unless something of the kind
20 that we recommend takes place, it is here to stay.

21 COMMISSIONER LEMAN: Is this a case of there
22 ought to be a law, or what?

23 MR. SHAW: No, the suggestion that we make,
24 through the Commission rather indirectly to the banks,
25 is that they might like to have some discussions about
26 it.

27 COMMISSIONER MACKINTOSH: Well, I have reason
28 to believe the banks may hear of this.

29 You also recommend, in a generous frame of
30 mind, the removal of the 6 per cent ceiling on bank



1 interest. Does this relate to the same desire for
2 flexibility of rates?

3 MR. SHAW: It does indeed, sir. During our
4 conversations with the banks at that particular time
5 which by coincidence coincided with the first change
6 that we had in the scale, the position was taken by
7 the banks that by reason of the fact that in a period of
8 very tight money when the banks might have every reason
9 to expect that they could have obtained a higher return
10 upon their loan resources, they were held to the 6 per
11 cent level. So, for that reason when the rates began
12 to decline, we felt there was some justification for
13 retaining the higher rate for a somewhat longer period
14 than would normally be warranted to make up for the
15 lost opportunities to the bank, had they not been on
16 a 6 per cent ceiling.

17 In addition to that we were inclined to take
18 the view that the reasons that existed for the original
19 imposition of this restriction were because in the first
20 instance the position was taken that the banks should
21 not loan at 7 per cent because if they did they were
22 incurring greater risks than they should take and,
23 secondly, that any rate higher than 7 per cent was a
24 rate that the agricultural community could not support.
25 These were two reasons cited in the MacMillan Report
26 of 1933. If those were the reasons for the imposition
27 initially we felt that they still existed, and we
28 take the position that this ceiling is anomalous and
29 presents an undue restriction on freedom of contract,
30 if you like. We felt that they/ought to be allowed to occupy



1 COMMISSIONER LEMAN: No ceiling at all, and
2 it is rather interesting to note in the report that
3 they recommend the ceiling be removed.

4 COMMISSIONER BROWN: Perhaps the bankers
5 prefer that we do not make a recommendation in case
6 we reduce it to five per cent!

7 COMMISSIONER MACKINTOSH: In paragraph 29
8 of that section you complain of the residual nature
9 of the chartered bank investment policy in that it
10 leads them to sell securities when the demand for
11 loans is high and buy securities when the demands
12 for loans is low. Now, admitting that the experience
13 of 1959 was a bit strenuous, is not that a normal
14 working of the market in the financial intermediaries?

15 MR. SHAW: First of all, we did not try
16 to make it sound too much like a complaint; we pointed
17 out that this was really what happened; that the
18 security markets -- and certainly this did happen
19 in 1959 -- were subject to pretty severe impacts as
20 the banks added reserves to look after the pressure
21 that was there on the part of their customers for added
22 loans, and we point out only that this does pass through
23 to the subsidiary markets and through them to the
24 dealers some pretty severe shocks from time to time.

25 We go on to point out that this applies
26 not only to their current deposits but to all deposits
27 including the steadily rising savings deposits.

28 COMMISSIONER MACKINTOSH: However, I would
29 take it that there is evidence that the chartered
30 banks were not the prime movers in this series of events?



1 MR. SHAW: No, we presume that is right.

2 COMMISSIONER LEMAN: What has it reached
3 now?

4 MR. SHAW: I think it is 5.65. What day
5 is it?

6 COMMISSIONER MACKINTOSH: I find also there
7 appears to me to be a contradiction in a couple of
8 the following paragraphs.

9 You speak of the tendency of the banks,
10 the chartered banks towards increasing liquidity in
11 their investments. You quote with some approval
12 the suggestion of the governor of the Bank of Canada
13 some years ago that you might look towards longer
14 investments in the light of the amount of their
15 savings profits, and then I am not sure whether you
16 recommend or not ---

17 MR. SHAW: May I interrupt you, sir?

18 COMMISSIONER MACKINTOSH: Yes.

19 MR. SHAW: We were very careful not to
20 make a recommendation on this point. We said there:

21 "This suggests as an avenue of exploration
22 the possibility that personal savings
23 deposits held by the Chartered Banks..." --

24 COMMISSIONER MACKINTOSH: I know you do
25 not make the recommendation there, but you did then
26 say that the banks continued to refrain from making
27 term loans?

28 MR. SHAW: That we did make a specific
29 reference to.
30



1 COMMISSIONER MACKINTOSH: It is not because
2 it is a longer term investment, according to your
3 previous statement. What is the reason for it?

4 MR. SHAW: We realized that there might
5 be some apparent contradiction there, although we do
6 not think that there is, but our objective is --
7 rather, shall we say that our approval of the present
8 arrangement and agreement amongst the banks to refrain
9 from making such term loans carries our full approval.
10 What we were concerned about the time before this
11 agreement came into effect was the steadily increasing
12 practice on the part of the chartered banks to negotiate
13 directly with corporate would-be borrowers; loans
14 for periods of repayment longer than the normal period
15 of that loan and for purposes which were clearly
16 capital purposes and taking on the full amount --
17 taking this as an investment for the amount of these
18 loans it made.

19 COMMISSIONER MACKINTOSH: That is the
20 alternative to the client issuing the securities.

21 MR. SHAW: Quite, and we took the position
22 that in many of these instances that the borrower
23 in normal circumstances would have entered the long
24 term market and gone through the normal underwritings
25 to the advantage of the borrower!

26 COMMISSIONER MACKINTOSH: At least!

27 COMMISSIONER GIBSON: On this same point,
28 on his yield of the banks making small term loans
29 under one-quarter million dollars ----
30



1 MR. SHAW: Our recommendation is term loans
2 beyond a reasonable amount.

3 COMMISSIONER GIBSON: I did notice that.
4 You do not express any view on that?

5 MR. SHAW: We take no exception to loans
6 of a reasonable amount under the circumstances. As
7 a matter of fact, I think you will find somewhere
8 else in our brief that in the small business area
9 there are comments as to the hope that the banks
10 might be able to look after ---

11 COMMISSIONER GIBSON: I did notice that,
12 and that is why I asked the question.

13 MR. SHAW: The emphasis is on size or
14 smallness.

15 COMMISSIONER MACKINTOSH: There were
16 a couple of sentences which I confess I did not
17 understand. In paragraph 58 of that section at
18 the beginning you say:

19 "There has been concern expressed in
20 recent years as to the responsibility
21 of the dealer in the placement of the
22 securities of 'near-banks'. The pressure
23 exerted within a firm to secure funds
24 for a client have, undoubtedly, resulted
25 in the placement of securities of dubious
26 quality."

27 I do not just understand what the mechanics of this
28 were, so to speak.

29 MR. SHAW: Well, this has to do with so-
30 called corporate paper; a market which has developed



1 and extended considerably in the last short while.

2 As I say, our interest is in the develop-
3 ment of this market and we recognize in many cases
4 that it is an advantage to the corporation, the borrower,
5 to give the accommodation which he values, although
6 I personally am not aware of any cases where it clearly
7 states that securities have been placed, but members
8 of my committee maintain that they were aware of such
9 instances.

10 The definition of the word "dubious" was
11 not too clear. However, as far as we are concerned
12 I think we feel that this is an area where great
13 care should be exercised; that a dealer who sets up
14 this type of paper should make available to the
15 lender the information which will enable him to measure
16 the quality of the loan that is being made, and I
17 am fearful as to where the relationship between the
18 dealer and the corporate bank may lead. The dealer
19 could make available accommodation to a corporate
20 client in some instances which might ultimately
21 lead to trouble.

22 COMMISSIONER MACKINTOSH: And when you
23 say "pressure within a firm" you mean pressure
24 within the dealer's firm?

25 MR. SHAW: That is right, pressure between
26 the dealer and his corporate clients.

27 The danger that we are concerned about is
28 that this type of loan accommodation as it might
29 be obtained by the corporate buyer at a time when
30 he had to protect himself in his own line of credit



1 with the bank, so that should it turn out that he
2 could not renew such a loan, he may find himself in
3 a position where his bank would be unwilling to provide
4 the funds to repay and it would cause an incident
5 in the market which he would very much like to avoid.
6 There has been to my knowledge no such instance so
7 far.

8 COMMISSIONER MACKINTOSH: I take it this
9 paragraph is an admonition to your own industry to
10 watch itself rather than a recommendation?

11 MR. SHAW: That is something for the
12 record --

13 MR. MILNER: It is exactly a similar
14 security to those provincial -- those short term
15 provincial notes where it would be a simple thing
16 from my point of view.

17 COMMISSIONER MACKINTOSH: Mergers with
18 the different agencies?

19 MR. MILNER: Yes, the corporation market
20 has been a very large one and a very sound market
21 in the long run for corporations as a whole, and
22 you are quite right to say that it is an admonition
23 to ourselves to be sure we do not go too far and
24 get one that cannot be repaid.

25 MR. SHAW: It may well be that the develop-
26 ment of the bank's acceptance of this market, which
27 got off to a start in rather an unfortunate climate
28 might obviate these dangers and provide this kind of
29 accommodation, but I do not know.

30 COMMISSIONER LEMAN: You reiterated this



1 morning the assertion that you are willing to take
2 full responsibility for the distribution of any kind
3 of security.

4 MR. MILNER: We take full responsibility.

5 COMMISSIONER LEMAN: Would there be any
6 situations, say, where this could be embarrassing or
7 that this is the case?

8 MR. MILNER: That is it exactly.

9 MR. ELY: I think I can add to this
10 because we do a large business in this type of thing.
11 I think most dealers probably have an approved list
12 of corporate borrowers for whom they will raise money,
13 but when it gets down to the dubious quality they
14 do not do it.

15 COMMISSIONER MACKINTOSH: Now, I have
16 another question on your recommendations. I would
17 like some further explanation of recommendation of
18 (3)(b) which says:

19 "...that there should be no further
20 extension, beyond the relatively few
21 cases of long standing which may exist,
22 of the inclusion of banks and syndicates
23 underwriting corporate securities for
24 resale to the public,"

25 That is at the end of the paragraph. Exactly what is
26 the problem there?

27 MR. SHAW: There is a further section to
28 that sentence which you didn't read:

29 " particularly where such inclusion would
30 place the bank in the dual position of banker



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1 and underwriter and where the sale of
2 corporate securities is for the income
3 bank loans."
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1 As a matter of fact, there are very few instances
2 where the chartered banks are members of corporate
3 underwriting syndicates. Those instances which do
4 exist have been in existence for a long time and were
5 entered into for very good reasons at the beginning.
6 We make no recommendations for changes in that area
7 and we have no reason to believe that the banks have
8 any ambition to restrain their activities in this
9 direction and we express the hope that they have no
10 such intention.

11 COMMISSIONER MACKINTOSH: I take it that
12 having admonished your own industry you are now
13 admonishing the banks?

14 MR. SHAW: We are telling them how happy we
15 are with the status quo.

16 COMMISSIONER BROWN: How about the present
17 restriction in the Bank Act of banks' names appearing
18 in them, in the advertising of underwriters?

19 MR. SHAW: We make some mention^{of} that in the
20 body of our appendix and as it now stands it is expressly
21 laid down that the name of any chartered bank may not
22 appear in the prospectus of its securities.

23 COMMISSIONER BROWN: But there are participating
24 securities -- it is in the Act that you should not,
25 but in your opinion is the Act right or not?

26 MR. SHAW: I am sorry you added that last bit,
27 but I was going to say that the reason they don't appear
28 is that the Act says they may not appear.

29 COMMISSIONER BROWN: The Act is up for discussion.

30 MR. SHAW: And we raised the question as to the



1 intent of that restriction at the time the Bank Act
2 was revised in 1934, or whenever it was. I wouldn't
3 care to express -- perhaps if you restate the question.

4 COMMISSIONER BROWN: Let me restate the question.
5 In view of the fact that banks are participating in
6 such underwritings and they are members of the syndicates,
7 do you think that the Act should be amended or that
8 their names could or should appear in the advertisements?

9 MR. SHAW: To speak personally, I think that
10 the participants -- all of the participants in these
11 syndicates should be prepared to make themselves
12 known as members of the syndicate, that is a personal
13 view.

14 COMMISSIONER BROWN: Do any of the other
15 representatives here care to express a personal view?

16 MR. ELY: I will subscribe to that; they
17 have a liability and there is no reason in the world
18 why their names shouldn't appear in the Act.

19 MR. KINNEAR: That is the part on full
20 disclosure.

21 COMMISSIONER BROWN: Is there an association
22 viewpoint?

23 MR. MILNER: It was never brought up in our
24 discussions. I think if you were to canvass the industry
25 as a whole there would be a divided opinion as to
26 whether in the revision of the Act, whether they should
27 be permitted to, but you have heard some of the people
28 here say that they would be quite prepared to not
29 exactly recommend it but have no objection to that
30 appearing.



1 COMMISSIONER BROWN: You apparently had some
2 views at the time on your mind or some arguments
3 against having the names appear; would you care to
4 state them?

5 MR. MILNER: Well, I think now we have attempted
6 in all instances to keep anything selfish out of our
7 presentation.
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1 I think it would encourage the banks to do more of
2 our business than they are doing now, and they are doing
3 a fair amount at the present time, as we well know.

4 COMMISSIONER BROWN: Do you think this might
5 encourage other potential borrowers to approach banks?

6 MR. MILNER: To attempt to get them for their
7 name.

8 COMMISSIONER BROWN: Are there any other points
9 of view that there could be expressed?

10 MR. COX: I , for one, as a personal observation,
11 would not like to have the banks' names appear. I
12 agree that I think it would encourage them to try and
13 do more business in this direction. I think it may
14 encourage some borrowers to go directly to them to
15 obtain their funds from possibly an underwriting or
16 term loan. There is one item on term loans that perhaps
17 should be mentioned, that they are potentially inflationary
18 to the extent that a bank grants a credit or deposit
19 to the borrower and it is not matched by withdrawal
20 in the banking system of savings from accounts of
21 individuals who might be buying the securities.

22 COMMISSIONER GIBSON: But if there is no
23 increase in the money supply, why is a term loan more
24 inflationary than a short-term loan?

25 MR. COX: It is not, except it stays as
26 a permanent part of the supply until it is repaid.

27 COMMISSIONER GIBSON: It does not turn over
28 as much.

29 MR. COX: If you loan money for 5 years it
30 is likely to be there for five years. If you loan it



1 through the normal banking procedure, it is likely
2 to be repaid, but if you continue this thing ---

3 COMMISSIONER GIBSON: Well, if it adds to
4 the money supply, what you say is obviously correct;
5 if it does not add to it I cannot see it has any effect
6 on any kind of loan.

7 MR. COX: Well, I understood this was the
8 thinking of the Governor of the Bank when he started
9 proposing term loans.

10 COMMISSIONER GIBSON: That is was inflationary?

11 MR. COX: Yes, and that, it could lead to ---

12 COMMISSIONER GIBSON: In proposing the term
13 loan?

14 MR. COX: Yes. Isn't that your recollection
15 of it?

16 COMMISSIONER GIBSON: I think this was perhaps
17 at an inflationary time.

18 MR. COX: Yes.

19 COMMISSIONER GIBSON: And I think his thinking
20 was perhaps he wanted the banks either to borrow it
21 and long-term borrowers to go out and borrow on the
22 market, and obviously he wanted to restrain any increase
23 on bank credit, but just the act of making a term loan,
24 if there is no change in the money supply, how can that
25 ---

26 MR. COX: No, if there is no change, but there
27 is a chance there will be, is there not?

28 COMMISSIONER GIBSON: It depends on what the
29 central bank does.

30 COMMISSIONER MACKINTOSH: I have one or two



1 questions on stocks, some part of which has been
2 covered already. Incidentally, I find a couple of
3 sentences in an earlier section which I think convey
4 an impression other than intended. Back in Section I,
5 paragraph 12, a couple of sentences of which the misleading
6 part is clear if I reverse it. It says: "The small
7 investor depends almost entirely upon his investment
8 dealer... etc.,... for guidance within his investments
9 ..."

10 Immediately before that: "Very rarely will
11 the small investor be found who owns one or two good
12 investment grade stocks."

13 MR. KINNEAR: I was afraid you would catch
14 that, sir.

15 COMMISSIONER MACKINTOSH: I gather what you
16 mean is that the job of educating the small investor
17 and bringing him up to some degree of sophistication
18 is a difficult job?

19 MR. KINNEAR: That was not worded that way when
20 we saw the last draft. How it got this way, I am unable
21 to explain.

22 COMMISSIONER MACKINTOSH: Another thing I
23 wanted to ask about: You have considerable reference
24 here to the degree to which institutions buy stocks.
25 How far do you think legislation, regulation, bookkeeping,
26 convention, the form of trustee laws, conventions of
27 the life insurance investment departments and valuation
28 requirements -- how far do they inhibit the number of
29 these institutions or bias their actions in respect
30 of purchase of stocks? Are there definite barriers, so



1 to speak, in the market.

2 MR. CRETZIANU: Do I understand that your
3 question is, are life insurance, for instance, prevented
4 by some of the regulations to invest in equities?
5 There is a limit of 15 per cent.

6 COMMISSIONER MACKINTOSH: Oh yes, I know that,
7 but almost none of them are at that.

8 MR. CRETZIANU: No, far from it.

9 COMMISSIONER MACKINTOSH: More precisely, do
10 you think that trustee laws, laws governing trustee
11 funds ought to be widened?

12 MR. CRETZIANU: Well, they have already been
13 liberalized. I don't think that this is any obstacle
14 at the moment.

15 COMMISSIONER MACKINTOSH: You don't think it
16 is any obstacle?

17 MR. CRETZIANU: No.

18 COMMISSIONER BROWN: Well, could we clarify
19 that: Have trustee acts been liberalized so they
20 can buy common stocks?

21 MR. MILNER: Not as such, but the legal
22 practice today -- the lawyers in drawing up wills
23 have covered it pretty extensively. In other words,
24 the modern will no longer restricts investments to
25 securities.

26 COMMISSIONER BROWN: That is not quite the
27 same thing.

28 COMMISSIONER MACKINTOSH: Surely, it was
29 always true that a man could make his will as he liked?

30 MR. MILNER: Yes, but it was only the last



20 or 15 years that there has been this marked change in the types of wills that the trust companies recommend and lawyers recommend just to be sure that they are not restricted completely to the trustee acts in the various provinces.

COMMISSIONER BROWN: As I understood Dr. Mackintosh's question, it was whether in your opinion the trustee acts should be liberalized to permit this investment in equities?

MR. CRETZIANU: I don't have the text here, but there have been relaxations on investment restrictions covering trustee pension funds.

COMMISSIONER BROWN: Trustee pension funds?

MR. CRETZIANU: Yes.

COMMISSIONER BROWN: We are talking about the trustee act for trustees.

MR. CRETZIANU: No, I was meaning the trustee pension funds. There have also been various measures to permit the sale of variable annuities of life insurance companies which is also a movement in the same direction.

MR. MILNER: To answer the specific question, trustee acts of the various provinces -- and this is purely a person viewpoint -- but, in my opinion, I think the present restrictions probably help a lot of the very small people to conserve their money. In other words, the people who don't want to come under the trustee act have plenty of ways of avoiding it: In the actual wills, as I say, is the simplest method, but I would rather tend to leave the trustee acts where they are. I would like to have somebody else comment on that.



1 COMMISSIONER MACKINTOSH: I am not particularly
2 concerned with the trustee act. I wondered if the
3 industry feels there are rigidities which prevent
4 the market from being as free as it might.

5 MR. WADDS: I am inclined to agree with you
6 as far as the small individual is concerned. I think
7 in some cases of estates administered by trust companies,
8 and where they were set up several years ago, there
9 could be more liquidity in this by a change in the
10 trustee act. For people who derive a living from these
11 estates, I have seen legal restrictions placed upon
12 them which resulted in a certain amount of hardship,
13 and that is the only reason I would say there would
14 be some sense in taking some of the restrictions off.

15 COMMISSIONER MACKINTOSH: If I could ask a
16 last question as the time of adjournment is approaching,
17 do you encounter reluctance to show a bookkeeping loss
18 as a barrier to complete freedom of access to the
19 market?

20 MR. SHAW: In terms of equity?

21 COMMISSIONER MACKINTOSH: Yes -- well, not
22 only equity.

23 MR. SHAW: I think it could be safely said
24 that the life insurance companies, some of them, in
25 their internal policies prevent their investment
26 department from investing freely if there is a loan
27 involved in bonds, but the equity holdings of life
28 companies are not large enough to make it a significant
29 factor there.

30 COMMISSIONER MACKINTOSH: Thank you.



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THE CHAIRMAN: We will adjourn now until
8.45 tomorrow morning.
--- Adjournment

Royal Commission on Banking and Finance

The Investment Dealers' Association
of Canada. (concluded).

Hearings
held at

OTTAWA

Vol.

27

(Relates to Brief at Vol. 22A)

Date.

July 12, 1962



Official Reporters
J. J. Nethercut and R. J. Young
Toronto, Ont.



ROYAL COMMISSION ON BANKING

AND FINANCE

Hearings held at Ottawa,
Ontario, on Thursday,
July 12th, 1962.

THE COMMISSION

The Honourable Dana Harris Porter
Chief Justice of Ontario
Toronto, Ontario - Chairman

Mr. W. Thomas Brown, M.B.E.
Investment Dealer
Vancouver, British Columbia

Mr. James Douglas Gibson, O.B.E.
Banker
Toronto, Ontario

Mr. Gordon L. Harrold
Agriculturalist
Calgary, Alberta

Mr. Paul H. Leman
Corporation Executive
Montreal, Quebec

Mr. John C. MacKeen
Corporation Executive
Halifax, Nova Scotia

Dr. W.A. Mackintosh
Vice-Chancellor
Queen's University
Kingston, Ontario

Mr. H.A. Hampson - Secretary

Mr. Gilles Mercure - Joint Secretary



Ottawa, Ontario,
Thursday, July 12, 1962.

--- Upon resuming at 8.45 A.M.

THE CHAIRMAN: The proceedings will now resume.

COMMISSIONER GIBSON: Gentlemen, yesterday we asked quite a lot of questions about the operations of your business and today we are going to go to a bit broader field and ask you questions about your views on monetary and financial policies.

I propose to start by asking a few questions about exchange policy and international capital movements and since you have made your recommendations here, of course, the official exchange policy has changed. In Recommendation (4) you ask us to consider the desirability of a pegged rate. We have a pegged rate. What we would like is to get your views on the significance for monetary policy of having a pegged rate and its effect in the basic picture, the significance for monetary policy and for the securities market. Would any of your members care to comment on this?

MR. MILNER: Mr. Gibson, I am going to ask Mr. Cox to speak on this subject.

MR. COX: Mr. Commissioner, the first thing that perhaps arises from having a pegged rate is the Bank of Canada's policy can no longer be dictated by what they feel is appropriate action from internal economic conditions. They have also got to regulate interest rates to take care of capital flows. This, of course, I suppose could lead to a very peculiar



1 situation where in a recession you would have to have
2 higher interest rates and perhaps conversely.

3 COMMISSIONER GIBSON: In other words, it might
4 be what one would describe as a perverse reaction?

5 MR. COX: Yes.

6 COMMISSIONER GIBSON: Do you envisage this?

7 MR. COX: I never was very good at looking
8 forward into what might happen. This perhaps is the
9 thing that we have the greatest difficulty with in our
10 business -- the difficulty of forecasting and it perhaps
11 is made more difficult now because the bank has to
12 serve two masters instead of one under this policy.

13 COMMISSIONER GIBSON: Do you see wider variations
14 in interest rates as the result of having pegged the
15 exchange rate this year, that is, other things being
16 equal?

17 MR. COX: I don't know about wider. We have
18 had some pretty wide swings already in the past few
19 years. These swings might become more frequent rather
20 than wider but this is just a personal view of my
21 own. I do not know how you could answer that question
22 with any degree of accuracy.

23 COMMISSIONER GIBSON: What you were implying
24 was it put more emphasis on changes in rates?.

25 MR. COX: Yes.

26 COMMISSIONER GIBSON: Do you see any other
27 implications of a fixed exchange rate?

28 MR. COX: Not off-hand. Perhaps somebody else
29 would have a few thoughts on the matter.

30 COMMISSIONER GIBSON: Would you say, for example,



1 to be more specific that with the fixed rate our
2 security markets would be more likely to move in line
3 with those in the United States or less in line with
4 those in the United States?.

5 MR. COX: I think they would more inclined to
6 move in line with the United States markets. They
7 always have but perhaps more so now.

8 MR. HUNTER: If I may, Mr. President, I
9 think experience has shown us that where there has
10 been stability for any lengthy time the Americans are
11 more inclined to buy our interest bearing securities.
12 That applied even when the dollar was selling at a high
13 level and I think now we have come to a fixed rate
14 and one can become convinced that that can be maintained,
15 it is altogether likely they will come to this market
16 and start an inflow of capital. There was some
17 indication of that recently.

18 COMMISSIONER GIBSON: You are talking of the
19 long-term operations?

20 MR. HUNTER: Which are the important ones.
21 The short-term ones do not help us in the end.

22 COMMISSIONER GIBSON: I would like to go a
23 little farther. You emphasize in your recommendations
24 the importance of allowing free movement of capital
25 in Canada from abroad. This is in Recommendations (5),
26 (6) and (7) and you use the words: "Repeated access
27 to the Canadian market" and you also suggest it would
28 be a good thing if this inflow of capital came in the
29 form of debt securities rather than equity investment.
30 In connection with this what is your view as to our



1 tendency to encourage capital in the present decade
2 as compared to the last decade -- more or less?

3 MR. COX: Well, that is a pretty hard one
4 to answer, I think Mr. Commissioner.

5 COMMISSIONER GIBSON: Very important, though.

6 MR. COX: Well, we presumably will continue
7 to require more capital than we are able to generate
8 internally but we also have excess plant capacity and
9 it becomes a question as to whether this is as
10 desirable a country for a foreigner to invest in as it
11 was in the early 1950's -- 10 years ago. I do not
12 know that I can say much on this subject. I am not
13 an expert by any means on this subject. Perhaps
14 some of the others here would have some comments to
15 make.

16 COMMISSIONER GIBSON: We have been very
17 dependent on foreign capital in the 1950's, particularly
18 the latter half?

19 MR. COX: Yes.

20 COMMISSIONER GIBSON: It would be very interest-
21 ing to have your views as to whether this degree of
22 dependency is likely to continue?

23 MR. MILNER: The great influx of foreign
24 capital into this country came in the last 15 years,
25 particularly where there was this confidence all over
26 the world that Canada had a very great growth potential,
27 a greater growth potential in North America than the
28 United States but I think some of the actions that
29 have occurred in the past two or three years have
30 disillusioned a lot of so-called foreign investors as to



1 the stability of this country. But basically the
2 reasons that brought the money here, say, 15 years
3 ago are still here. If the monetary policy could be
4 adjusted to meet the economic conditions that exist
5 today I would look forward to more capital coming in
6 again and I think if we are going to have a growth like
7 we had since the past war I do not think it is possible
8 to generate that amount of money in Canada.

9 COMMISSIONER GIBSON: In other words you are
10 saying today the rest of the world do not want to put
11 more money in here for the time being but we still need
12 it?

13 MR. MILNER: We still need it.

14 COMMISSIONER GIBSON: Do we need it on the same
15 relative scale that we needed it in the last half of
16 the 1950's?

17 MR. MILNER: I should hope so.

18 COMMISSIONER GIBSON: As much as we needed it
19 in the 50's?

20 MR. HUNTER: We will need it to balance our
21 foreign exchange picture. Equity capital may not want
22 to come to Canada as much as it has in the past over
23 the years but if our interest rates are sufficiently
24 attractive and if we follow through the measures that
25 have been suggested it is quite conceivable there
26 could be a very strong demand for our interest bearing
27 securities which create quite an inflow of capital.

28 COMMISSIONER GIBSON: Well, let us look at it
29 the other way. Do you think we can reasonably expect
30 to generate a sufficient level of dollar earnings to



1 pay these increasing service requirements for foreign
2 capital over the next few years? Is that a reasonable
3 expectation or is it not?

4 MR. SHAW: Aren't we dealing with a somewhat
5 different set of circumstances now, Mr. Commissioner,
6 than during the period that you have alluded to?
7 We went through a period where we were doing on the
8 investment sector of our economy on our public and
9 private investment stocks more than the rate of over
10 25 per cent of the gross national product. While that
11 was going on obviously that sort of programme could not
12 have been maintained out of our own resources. That
13 sort of a programme was probably not initiated entirely
14 by our own thinking. The need obviously is not going
15 to be as great once we have got that heavy programme
16 of investments completed. Surely we must be approaching
17 a period where the results of that investment will
18 begin to make their contribution to the problem, that
19 a good deal of this productive equipment that was put
20 into place with that kind of money must soon -- although
21 admittedly not as quickly as some of the investors might
22 have hoped -- that this must soon begin to make its
23 contribution in the way of productivity and internally
24 generate funds so that in the future we could very well
25 not have the need for quite the heavy proportion or
26 percentage of our capital investment to come to us
27 from outside.

28 COMMISSIONER GIBSON: Would you think it
29 reasonable to estimate in terms of a need half as great
30 as the average in the 1950's or something of that order?



1 MR. SHAW: I think we have made the transition
2 so quickly from one side to the other, we were in the
3 position of heavy inflow and suddenly we are in the
4 position where we are now on balance on an outflow
5 position. It would be presumptuous to suggest any
6 measure of degree of normal conditions. All I would
7 like to suggest is that the need is not likely to
8 be as great as the experience has been in the past and
9 we will have a better chance of generating a better
10 proportion of the capital needed in this country
11 internally from here on than perhaps would have been
12 the case from 1946 to 1956 or 1957.

13 COMMISSIONER BROWN: Recommendation No. (6)
14 there says:

15 "...that, to the extent that it is
16 necessary or desirable to import capital from
17 foreign countries, Government of Canada policies
18 be established which will encourage the
19 purchase by foreigners of debt securities
20 rather than equity investments of all kind."
21 How are you going to measure this "necessary or desirable"?

22 MR. COX: Well, "necessary" would be the result
23 of our trade balances and our invested items -- what is
24 the balancing item. That would be the necessary item,
25 would it not?

26 COMMISSIONER BROWN: What are the long-term
27 implications for borrowing to meet your current debt
28 services?

29 MR. COX: This, of course, depends upon our
30 ability to pay it, I presume, when translated into



1 what kind of trade balances are we going to have.
2 Are we going to be successful in stimulating exports
3 to the point where we have a favourable trade balance?
4 This would look after the important part of the complete
5 balance of payments. If we do not do that I think
6 we are getting in over our heads.

7 COMMISSIONER BROWN: At the moment we need
8 several hundred millions of dollars to service our
9 present debt securities?

10 MR. COX: Yes.

11 COMMISSIONER BROWN: To the extent that we
12 cover our requirements for further borrowing are we
13 not making a greater problem for ourselves?

14 MR. COX: I think we are if we do not manage
15 to counteract at the same degree, to a considerable
16 degree, by meeting our trade balance.

17 COMMISSIONER BROWN: What policy do you suggest
18 we ought to adopt to accomplish this?

19 MR. COX: Well, it becomes a question of
20 productivity, I would think, how competitive are we
21 in world markets and a lot of these things we cannot
22 entirely control. The other question is are people
23 abroad going to require what we can produce. It is
24 only a question of price at which we can produce it
25 but will they want it. Is there a market, in other
26 words.

27 COMMISSIONER BROWN: You are suggesting a
28 lot of this is entirely beyond our control?

29 MR. COX: A lot of it. I think anything the
30 Government can do to encourage, stimulate and provide us



1 with a suitable climate which would enable us to become
2 more able to produce what the world wants from us the
3 better our chance of getting our house in order.

4 COMMISSIONER GIBSON: Now, to return to the
5 investment point, you ask us, that is, the Commission,
6 to recommend to maintain a favourable investment climate
7 in Canada to be sure that this will be available when
8 needed. Would you be a little more specific about the
9 kind of policies that are required to maintain a
10 favourable investment climate?

11 MR. COX: We have had such an about-face
12 from the climate that did exist, that encouraged the
13 inflow of capital, things like withholding taxes on
14 fixed income securities and on balance budgets and things
15 like this, these all hinder the possibility or likelihood
16 of inflow. I would think the Government should take some
17 steps as soon as possible to remove these obstacles.
18 Perhaps we are moving in that direction now in the late
19 June announcement from the Government.

20 COMMISSIONER GIBSON: Specifically withholding
21 tax and the budget deficit, in your view, is too large?

22 MR. COX: Yes, and it keeps on as a deficit
23 regardless of what kind of business conditions exist
24 in the country.

25 COMMISSIONER GIBSON: Well, this is not
26 altogether true. Since 1957 and 1958, let us, we
27 have not had a high level of business activity in
28 relation to our employment?

29 MR. COX: No.

30 COMMISSIONER GIBSON: So this is a period that



1 there has been a pressure. Right through this period
2 we have had a rate of unemployment higher than at any
3 time since the war?

4 MR. COX: I think that is true but looking at
5 it from the other point of view we have had a couple
6 of complete business cycles in that area and now we
7 are making some progress in current dollar treatment.

8 COMMISSIONER GIBSON: We made some in 1961.
9 Up to then we were just going like this (indicating)
10 for four years?

11 MR. COX: Yes.

12 COMMISSIONER GIBSON: Are there any other
13 thoughts you have about the favourable investment
14 climate?

15 MR. COX: Well, taxation in general, of course.
16 I think this is something that should be thoroughly
17 studied and investigated from the basis for providing
18 greater incentives.

19 COMMISSIONER GIBSON: Part of this recommendation
20 -- or actually it is in Recommendation (6) is we produce
21 the kind of atmosphere or climate to encourage the
22 purchase by foreigners of debt securities. Would you
23 like to talk about it in those terms? First, why
24 do you make that recommendation?

25 MR. COX: Mr. Milner, would you like to talk
26 on that?

27 MR. MILNER: Mr. Gibson, there has been a lot
28 of publicity given in the past four or five years to
29 the effect of a number of our larger corporations,
30 the control of them passing into foreign hands and I



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1 think probably the chief objection to the passing into
2 foreign hands is the fact that if they are branches of,
3 let us say, American concerns it rather hinders the
4 possibility for research activities in Canada. The
5 research is usually done at the source rather than
6 in the country that they are operating in as a branch
7 subsidiary and one of our troubles has been -- and
8 especially in secondary industries of this country
9 is probably the lack of sufficient skills and the right
10 kind of people to go into it.



1 I think that basically the problem is
2 not part of your actual, whatever you call it.

3 COMMISSIONER GIBSON: The terms of reference?

4 MR. MILNER: The terms of reference. Our
5 taxation has not been seriously looked at for a number
6 of years. In fact, it has been done in bits and pieces
7 over the last 25 years. Surely the right answer is
8 to thoroughly examine the taxation picture, and not
9 by means of a Royal Commission which would take three
10 years to complete, and I say that with reference to a
11 viewpoint of urgency.

12 What we need to do today is to encourage
13 industries in this country to become competitive in
14 world trade.

15 I think one of the finest things that has
16 been done recently was the formation of the productivity
17 council. I think it is most unfortunate that the
18 government in its judgment did not put labour in its
19 proper form on the productivity council. Whether
20 that can be corrected or not, I doubt. What has been
21 the success and great resurgence in Europe unquestionably
22 is the result of getting government, labour and
23 management to work together. If we could attack this
24 problem from the source rather than in the other way,
25 I think the results would be much better. If this
26 country was more economically sound I feel we would
27 have no problem in getting good money or any other
28 kind of money.

29 I feel that we have a great loss of money
30 as a result of the difficulties in this country of



1 accomplishing mergers of companies. This again
2 involves a question of pure taxation. We have a
3 Federal Companies Act and Provincial Companies Acts
4 but I would suggest we would be much better off in
5 designing these acts in such a way as to facilitate
6 the creation of larger companies rather than smaller
7 companies. I do not mean to suggest that we should
8 merge Eatons and Simpsons, or Imperial Oil and British
9 American Oil, but in the echelon below that
10 I suggest small companies would be more efficient if
11 they became larger companies. I would be the first
12 one to admit that this would affect unemployment or
13 employment, but at the end of a reasonable period
14 of time, say a year or so, if we had more successful
15 smaller companies, I think the unemployment situation
16 would take care of itself.

17 COMMISSIONER GIBSON: You are ranging
18 around and past the borders of our specific reference.
19 What do you feel the investment dealers could do
20 to promote this business of selling debt securities
21 abroad? A number of the large members of your
22 Association have operations in New York. Is this
23 something you feel that the members of the Association
24 could make a fairly major contribution towards?

25 MR. MILNER: Mr. Wadds, would you care
26 to answer that?

27 MR. WADDIS: I would say, sir, that I think
28 the image of our government in this country abroad
29 has a national importance. I have a feeling that
30 until the feeling that Canada has a stable and sound



1 economy returns to foreign buyers of securities that
2 our operations in foreign markets are going to be
3 somewhat restricted. This is to a large extent
4 a psychological thing rather than a question of
5 dollars and cents. There is a resentment right now
6 towards the whole Canadian economy and market, and
7 unless we are prepared to sell securities at almost
8 penalty rates in the United States, we will find
9 it rather difficult to overcome this feeling of
10 resentment toward those things which have occurred
11 in this country in the past two years.

12 COMMISSIONER BROWN: Could you be more
13 specific about the resentments?

14 MR. WADDS: Certainly the prime one
15 was the taking over of the British Columbia Electric
16 Company. A second resentment is directed toward
17 the deficit financing that has taken place in this
18 country for some years. I should also mention the
19 fact that today we have a disturbed political
20 situation at the federal level, and we also have
21 mechanical problems created by such things as the
22 withholding tax. There is certainly a resentment
23 toward the nationalism which we witnessed when this
24 holding tax was put on. All of those things have
25 destroyed the confidence of foreign investment.

26 MR. HARRIS: There is one thing that
27 frightens me at the present time. We look at our
28 unemployment in Canada, but I suggest that similarly
29 in the United States they are concerned with American
30 problems relating to money outside of that country.



1 There is now a program of moral persuasion in the United
2 States in an attempt to restrict Americans putting
3 short term money out of the country.

4 COMMISSIONER GIBSON: Short term money did
5 you say? You do not refer to long term money?

6 MR. HARRIS: Some of this money has
7 recently gone into the long term field, but there
8 is a definite feeling that the flow of money should
9 be kept in the United States if at all possible.
10 This in a manner of speaking is a factor which has
11 developed within the last year or so, and is something
12 over which we have no control. I am rather frightened
13 by the prospect of the effect of this program, certainly
14 in respect to short term money. In spite of the
15 interest rates, and this seems to be the excuse, short
16 term funds have not been coming in at the rate at
17 which one might ^{have} expected within the last few months.

18 COMMISSIONER GIBSON: Is that why you put
19 the emphasis on recommendation number seven concerning
20 the withholding tax on short term money? I wondered
21 why it was applied to short term money here?

22 MR. HARRIS: I agree that you cannot take
23 it off one and leave it on the other. I believe you
24 must have a concerted policy in this regard.

25 On the money market through interest rate
26 changes you can move capital back and forth quite easily,
27 but the withholding tax has been a problem with which
28 we have had to deal. Our markets are very small and
29 it is only in respect to government bonds and treasury
30 bills that we have had an adequate supply, and I note that



1 we have moved a substantial amount of funds in that
2 regard. Certainly with respect to treasury bills
3 where the taxes are imposed at the time of issue
4 rather than at maturity/^{it}has created a problem in
5 mechanics, although perhaps a nuisance problem.

6 COMMISSIONER GIBSON: You are suggesting
7 that they be removed in the short end?

8 MR. HARRIS: I was thinking at the
9 present time they should be removed in the short end,
10 yes, although they should be removed in all categories.

11 COMMISSIONER GIBSON: Supposing they could
12 not be removed in all categories, you would then
13 recommend that they be taken off the short end? If
14 so, how do you fix this problem from the mechanical
15 point of view? Where do you draw your line?

16 MR. HARRIS: I draw the line on the shorts.
17 When this brief was written the situation was a little
18 different to what it is now from an economic stand-
19 point. We did not have a financial crisis such as
20 has since developed. Secondly, and this was suggested
21 as far as the short end of the market is concerned,
22 our present situation, and I think that we would be
23 unanimous in this suggestion, that the withholding
24 tax legislation should be looked into. This is a
25 nuisance tax. It is not levied on everybody. As
26 you know, there are only certain groups such as those
27 of a religious character, educational and scientific
28 bodies that do not pay that withholding tax. Corporations
29 can lay off the withholding tax against internal taxation.
30 It is basically only levelled on accounts such as state



1 funds, or something like that, or pension funds which
2 in the past have been substantial ^{buyers} ~~borrowers~~ in Canada
3 of securities both internal and external. This is
4 not a particularly equitable piece of legislation and
5 represents mainly a nuisance tax.

6 COMMISSIONER GIBSON: So you are objecting
7 to it on two grounds; one that you do not like the tax
8 and, secondly, that the incidence is uneven?

9 MR. HARRIS: That is quite true. This
10 is one of the difficult taxes. Although people often
11 can recapture the tax they are discouraged from doing
12 so because of the trouble involved in going through
13 the motions. They feel it is just too difficult
14 to bother with.

15 COMMISSIONER BROWN: I would just like to
16 explore some of these resentments that you talked about,
17 particularly with reference to your recommendation that
18 this Commission make some suggestions as to how these
19 can be handled.

20 First of all, in regard to the British
21 Columbia Electric takeover. Is the resentment directed
22 toward the actual takeover or the method of takeover?

23 MR. HARRIS: I would say it is largely
24 directed toward the manner in which it was done.

25 COMMISSIONER BROWN: Now, British Columbia
26 has not been the only province that has been making
27 suggestions along this line.

28 MR. HARRIS: I would say American investors
29 are well aware of the other rumblings from the other
30 provinces in regard to the taking over of utilities,



1 but this is the only province that has done so to date,
2 and the manner by which it was accomplished is definitely
3 not popular in the United States.

4 COMMISSIONER BROWN: What recommendation would
5 you make in line with preventing this type of thing
6 happening? You made a recommendation regarding certain
7 tax anomalies which should be removed.

8 MR. HARRIS: I would agree with Mr. Milner's
9 redistribution suggestion.

10 MR. MILNER: Public utilities with particular
11 reference to power utilities, because power is generated
12 within the province in practically all cases -- there
13 is a bit of export between provinces -- with the
14 exception of the Bell Telephone Company, which is in
15 a different category being a national company, it is
16 felt very strongly that could be considered as provincial
17 assets and therefore belong to the provinces. I think
18 there has been a great amount of publicity given to
19 this situation.

20 In regard to the taxation part of this problem
21 we suggest that the government should look into the
22 situation and devise some method of reimbursing the
23 provinces in respect to federal taxation which is involved
24 as far as power companies are concerned. We hope that
25 such a system would eliminate the reasons which are
26 used publicly for taking over power companies. We
27 do not believe that it is in the best interests of
28 this country to have confiscation of private enterprise
29 in any shape or form, particularly done without
30 arbitration.



1 COMMISSIONER BROWN: Yes, I was going to say
2 that you used the word "confiscation". Has there
3 been any confiscation as such?

4 MR. MILNER: Without arbitration it is
5 all confiscation. They simply fix a value -- their
6 own value -- and pay the shareholders that amount
7 of money.

8 COMMISSIONER BROWN: I do not think you
9 can claim that this has an effect on debt securities.

10 MR. MILNER: I am not so sure today that
11 a British Columbia Electric bond would not sell higher
12 than a province of British Columbia bond with guarantee.

13 MR. COX: This changes the investor's
14 portfolio around. He thinks he has got a public
15 utility bond and all of a sudden he finds that he
16 has a public bond which he may or may not want.

17 MR. HUNTER: British Columbia is part
18 of Canada as far as this is concerned in the investor's
19 mind, and he comes to look at all of our securities
20 in the same light as he regards British Columbia as
21 Canada.

22 MR. COX: I have been rather surprised
23 in speaking to American investors regarding their
24 concern over that expropriation. They seem to be
25 much more concerned than Canadian investors who
26 also hold the debt instruments. They are much more
27 vocal about the subject than our Canadian companies
28 have been.

29 COMMISSIONER BROWN: The next thing you
30 mentioned is deficit financing. What different policies



1 would you suggest the government should have followed
2 in the last few years when we had unemployment running
3 over 6 per cent?

4 MR. WADDS: I think Mr. Milner is prepared
5 to deal with that subject.

6 MR. MILNER: I am going to ask Mr. Ely to
7 speak in that regard if you do not mind.

8 MR. ELY: What is the question again,
9 Mr. Brown? I want to stick to the specific question.

10 COMMISSIONER BROWN: We were talking
11 about resentments abroad.

12 MR. ELY: Yes, I realize that.

13 COMMISSIONER BROWN: It has apparently
14 had an effect in the attitude toward Canadian debt
15 securities.

16 MR. ELY: Yes.

17 COMMISSIONER BROWN: One of the points
18 that was brought forward in this regard had reference
19 to deficit finance. I am assuming that this refers
20 to deficit financing at the federal level.

21 MR. ELY: That is right.

22 COMMISSIONER BROWN: My question is, during
23 the last few years when we have had unemployment
24 running over 6 per cent, what alternative forms of
25 government policy do you think should have been
26 implemented to satisfy the situation?

27 MR. ELY: Well, we have created an
28 atmosphere in this country, perhaps at the federal
29 level, that has inhibited the people investing their
30 money in this country, and deficits are one of the first



1 things brought up in this regard. There are perhaps
2 a few things that could have been done about this.
3 There has been extensive criticism regarding the type
4 of money that has been spent to look after unemployment.
5 Let me be specific as to one case which would probably
6 have saved us a lot of money and we would have had
7 a smaller deficit.

8 I am not too well versed in this, but this
9 is one of the things that has been brought up. On
10 both coasts there are large fishing industries. Over
11 the history of this country they have never been
12 compensated during the winter but they now are. I
13 do not know whether this should be attacked on a
14 political level or what level, but it seems to be one
15 area among others where the deficit could have been
16 cut down.

17 COMMISSIONER BROWN: Perhaps we should wait
18 for the Gill Commission report on that subject.

19 MR. ELY: That might well be. There is
20 no doubt about it that in this area there surely must
21 have been room for good business management so as
22 to bring our affairs into better balance which would
23 have set the climate for investors to put their money
24 in this country.

25 COMMISSIONER GIBSON: You are saying the
26 deficit was too large, not that there should not have
27 been one?

28 MR. ELY: I do not think one could find
29 fault with a small deficit, but the deficit was too
30 large.



1 THE CHAIRMAN: When would you say that it
2 became too large?

3 MR. ELY: I think it has been too large for
4 five years.

5 THE CHAIRMAN: One thing I noticed about
6 your recommendations in the brief which was prepared
7 before the last great crisis arose is that as far
8 as I can recall deficit financing is not one of the
9 points raised.

10 MR. ELY: One of the points that I raised,
11 Mr. Porter, is that our debt has increased by \$3
12 billion in the last five years.

13 THE CHAIRMAN: Yes, but in your recommendations
14 you have not mentioned that.

15 MR. MILNER: Yes, recommendation number one,
16 Your Honour, is directed toward that.

17 THE CHAIRMAN: Yes, I apologize.

18 COMMISSIONER BROWN: Let us deal with that
19 in a little more detail. It refers to surpluses in
20 years of prosperity.

21 MR. ELY: The conditions that have existed
22 in the last five years have not been depressive
23 in the main and did not deserve in our opinion a huge
24 increase in our national debt.

25 COMMISSIONER BROWN: Let us be a little
26 more specific about this because we should like to
27 get some concrete thoughts in this regard. I am
28 assuming that you are not suggesting that an unemploy-
29 ment rate of 6 per cent has to be accepted as normal?
30



1 MR. ELY: I do not think it should be
2 accepted. Some rate of unemployment has to be accepted,
3 and if we accept it then it might be dealt with in
4 a way that is perhaps not as expensive in this country.

5 COMMISSIONER BROWN: With a 6 per cent
6 unemployment figure, one cannot consider times to
7 be prosperous.

8 MR. MILNER: Mr. Brown, are you sure that
9 it is 6 per cent? I question that figure. I think
10 unemployment has been added to as a result of the
11 payment of benefits to people who have been employed.
12 There are bound to be abuses of a small nature.

13 COMMISSIONER MACKINTOSH: I do not think
14 the 6 per cent figure came from the Unemployment
15 Insurance Commission. I think it comes from the
16 Dominion Bureau of Statistics survey which has nothing
17 to do with the manner in which people are drawing
18 unemployment insurance benefits.



1 Now, you may argue that the availability of
2 insurance benefit in some cases leads people to be
3 unemployed rather than actively at work, but by and
4 large the 6 per cent doesn't cover people whom you
5 might say were not genuinely unemployed but merely
6 improperly drawing benefits, so that whether you think
7 it is a bit more or a bit less, I think 6 per cent
8 is real.

9 MR. MILLER: As accurate a figure as you could
10 get of the working people of this country, 6 per cent
11 of which -- I would still question whether that is
12 correct, Dr. Mackintosh. The abuses that have gone on
13 in the unemployment fund, which I say is bound to happen,
14 this might occur all over the world. I don't know
15 what the conditions are in other countries, but we
16 have seen so many instances of unemployment figures
17 that we are perfectly well aware are not correct.

18 COMMISSIONER GIBSON: I don't think we should
19 get into a discussion of the unemployment; all we are
20 really asking you is do you think that economic conditions
21 were such that it was necessary to run deficits, and
22 if so how much?

23 THE CHAIRMAN: After coming back to my question,
24 on reading this recommendation more carefully again,
25 I think I will have to withdraw it in part with my
26 apologies. They say that the deficit at the time this
27 was written is too large and that it is dangerous. You
28 don't do that; you soften it and say that the objectives
29 are the approximately equivalent budgetary deficits
30 which may have occurred in recession years -- if we are



1 going through certain recession years and the deficit
2 is being increased from year to year, the time for
3 surplus would come when the conditions change for the
4 better, according to this recommendation, I would think.

5 MR. BEATTY: The problem of unemployment has
6 been dealt with by several different bodies and given
7 great publicity. I understand that one of the factors
8 is lack of mobility of our labour forces. Another is
9 lack of skills in the unemployed and a third one is
10 that the Bladen Commission points up the fact that the
11 automotive industry is producing a great deal outside
12 the country to contribute to our balance of payment
13 troubles in importing parts, and so on, and we fail
14 to see why Federal Government deficits affect any of
15 these things unless they are active in tackling the
16 problems themselves.

17 THE CHAIRMAN: That is not what you have put
18 on the record here. This is the only point I am making;
19 you say now under present conditions that the budget
20 deficit is too great. One of the great sources of
21 our difficulties is that when you prepared this brief
22 prior to the monetary crisis that arose you didn't
23 put in that way, you put it in a much more softened
24 way.

25 MR. COX: I think this arose from the
26 suggestion that these large deficits were affecting
27 the foreign investors in this market.

28 THE CHAIRMAN: But you didn't say that at the
29 time.

30 MR. COX: I don't think we can say that this



1 financial crisis just happened; this has been building
2 up for several years.

3 THE CHAIRMAN: I may be wrong, it is some time
4 since I read the whole of this brief and I may not have
5 recollected some of the matters, but what I want to
6 make clear is this; that you say now that the deficit
7 is too large and it may be that people would agree
8 with that under present conditions and with a certain
9 amount of hindsight but it may be if I read it again
10 in the light of this particular point I might find you
11 have taken a stronger position than you seem to have
12 taken on recommendation No. 1, but if that is such a
13 serious item I would have thought it would have been
14 given the very greatest attention by your Association.

15 MR. SHAW: As I see the position, we think
16 the deficits have been unduly large measured against
17 the achievements that they can find for them in the
18 one area that the Commission seems to be directing
19 their questions to us about, and that is the area of
20 employment. It has been argued ---

21 COMMISSIONER GIBSON: Unemployment comes up
22 as a measure of lack of activity.

23 MR. SHAW: The Chairman has just mentioned
24 that these are recession years we have been going
25 through and if they are recession years -- and we say
26 in recession years we should have a deficit, so we
27 are not being consistent and these facts are all right
28 if we can accept that these are really recession years.
29 We admit they are years of high employment and also
30 point out that they are years of high employment and



1 high income, not necessarily recession years measured
2 by all other criteria you may use and I think our
3 concern is simply that in difficult periods if it is
4 necessary to build up a deficit, it calls for extreme
5 care to ensure that the monies that are being borrowed
6 are being put to the most effective use to deal with
7 the specific problem which we are tackling, and I think
8 that the point Mr. Milner made is a good one.

9 We didn't, perhaps, examine the national accounts
10 with the care we should have if we were going to pursue
11 this position, but we really have a feeling that a lot
12 of these expenditures which went into the deficit didn't
13 help very much in alleviating the unemployment problem.

14 THE CHAIRMAN: But aside from that, though,
15 wouldn't your position be that there is a certain point
16 where a deficit would be by its very size dangerous,
17 forgetting what it was used for?

18 MR. SHAW: Definitely, we feel the deficits
19 are a dangerous amount, and the bigger they get the
20 more dangerous they get.

21 THE CHAIRMAN: Well, is it necessary to relate
22 the amount of the deficit to the monies which were
23 derived from the deficit and to what they were used for.

24 MR. SHAW: We come back to the question that
25 was directed to us; what would we have done in the
26 circumstances in the face of the unemployment situation
27 that the country was contending with and we have attempted,
28 in perhaps not too effective a way, to submit some
29 suggestions, but it is a very difficult question to
30 look back and say that something different should have



1 been done, and I find a great many people today who
2 are complaining about the deficit who didn't complain
3 a few days before the crisis.

4 MR. HUNTER: May I read something:

5 "During periods of economic recession
6 and unemployment the practice of deficit
7 financing for the purpose of revitalizing
8 the economy has been generally accepted as
9 a necessary social obligation. However, during
10 the past 7 fiscal years ending March 31,
11 (1955-61 incl.) we have shown cash deficits
12 in six years (with a small surplus in 1957)
13 and the certainty of a deficit in the year
14 ending March 31, 1962. These deficits have
15 occurred despite periods of prosperity which
16 occurred during the years 1955-56, 1958-59
17 and 1961. These factors, together with the
18 concurrent increase in money supply which
19 has been necessary to finance the deficits,
20 have done a great deal to destroy the confidence
21 of investors in Government of Canada securities."

22 THE CHAIRMAN: What page is that?

23 MR. HUNTER: F.33.

24 COMMISSIONER BROWN: I think the point we are
25 making is this, that the first group suggested that
26 1951 was the first year of prosperity.

27 THE CHAIRMAN: I can see you have put yourselves
28 on record more definitely than I had thought.

29 MR. COX: I think perhaps there is another
30 point in this connection, the desirability of deficits



1 in a country like Canada. Mr. Towers went to considerable
2 lengths in 1939 to explain to the House Banking
3 Committee that in theory it might work in some countries
4 but it was highly unlikely to work in a country such
5 as Canada. It is fairly generally quoted in Section C
6 here, and our government chose to ignore Mr. Towers'
7 advice and went ahead with deficits and I think it is
8 a very open question whether the deficits have done
9 very much to cure the problem of unemployment in creating
10 an atmosphere where we could use our excess labour.

11 COMMISSIONER BROWN: I don't think there is
12 much point in labouring this much further. You have
13 said there were years of prosperity and other people
14 apparently don't agree with you and you have nothing
15 really concrete to suggest as to how this unemployment
16 might have been combatted other than the way it was,
17 except a general thesis that its deficits were acceptable
18 in that period, they were not acceptable in the degree
19 that was adopted.

20 MR. MILNER: Before you close this subject I
21 would like to make this comment. Let us go back five
22 years when the unemployment problem became acute.
23 Had the government taken other steps, such as reducing
24 corporation tax to encourage industry it probably
25 would have increased the deficits during that first
26 year but I would venture to say that had that worked
27 they would have had far less of an unemployment problem
28 today had we encouraged proper productivity deficit
29 spending in the way it was done.

30 MR. HUNTER: During this period the unemployment



1 fund has been virtually used up, which can be added
2 to the deficit.

3 COMMISSIONER GIBSON: This is getting into
4 the qualitative aspects and I think we are getting a
5 little away from our central interest here.

6 I want to change the subject a bit now and
7 switch to the subject of exchange in paragraph 37 in
8 Section C. The statement is made there that the Bank
9 of Canada has seldom operated in the futures market,
10 despite the fact that spot transactions may cause a
11 maldistribution of chartered bank cash or require
12 offsetting action. It then suggests that since there
13 are some seasonal movements of funds internationally
14 which tend to reverse themselves, transactions in futures
15 appear to be a simple course; simpler than not having
16 transactions in the futures. Would you care to elaborate
17 on this matter of operations in the futures market?

18 MR. COX: This, of course, has become outdated
19 because since May the Bank has been very active.

20 COMMISSIONER GIBSON: They have been active?

21 MR. COX: Yes.

22 COMMISSIONER GIBSON: In other words, the
23 policy has changed since the loan was paid?

24 MR. COX: Just prior to it, I think it was
25 April.

26 COMMISSIONER GIBSON: And you would say that this
27 statement was now out of date?

28 MR. COX: Well, it is true to the effect that
29 they never did, as far as we know, use the futures market
30 until April of this year, but since then their activities



1 have been very considerable. I don't know why we
2 are using it ---

3 COMMISSIONER GIBSON: You don't have any
4 opinions on that?

5 MR. COX: I don't know how we could, sir;
6 the Bank of Canada doesn't tell us why they are doing
7 things.

8 COMMISSIONER GIBSON: But you are working in
9 the market and are informed of things.

10 MR. COX: But we can be wrong in the opinions
11 we form.

12 COMMISSIONER GIBSON: But your view leading
13 up to the existing policy, whatever that is, is that
14 the Central Bank should operate in the futures exchange
15 market?

16 MR. COX: I don't know that I would use the
17 word "should"; I would say that the Bank of England
18 and other European central banks, as well as the
19 federal reserve, have found it a very useful thing to do.

20 COMMISSIONER GIBSON: Would you give us the
21 reasons why you think it is a useful thing to do?

22 MR. COX: In controlling the "hot" money
23 that can move on a hedged basis; operations in the
24 futures market can change the relationship between the
25 spot rate and the futures rate.

26 COMMISSIONER GIBSON: You say that the main
27 reason for a central bank going into the futures market
28 was in relation to movements of short-term capital
29 and not in relation to ordinary commercial transactions,
30 that the market will look after that itself?



1 MR. COX: I think it should.

2 MR. HARRIS: Recently, and this certainly
3 is one of the main factors in movements of short-term
4 funds because often the funds are not on a fully hedged
5 basis and it have been rather interesting recently the
6 way in which this has been handled. The Canadian banks
7 in New York have been able to pay for deposits as high
8 as 6-1/8 per cent because of the forward arrangements
9 and at a time of the present outflow of short-term
10 funds. Admittedly, they will come back after a certain
11 period and things will change, but there are times
12 when the market becomes very important in the movement
13 of short-term funds.

14 COMMISSIONER GIBSON: You are suggesting that
15 the Bank of Canada hasn't been active in the forward
16 market?

17 MR. HARRIS: They have been recently, but they
18 have found it difficult. I can't understand the
19 reason for this, but I think they were of such a size
20 and that it has become difficult to move in them at all
21 just in the last month or two, but at times this forward
22 market does have to be watched.

23 COMMISSIONER GIBSON: Are most of these short-
24 term movements that you speak of hedged?

25 MR. HARRIS: Normally short-term investments
26 in Canada, treasury bills and paper are hedged from the
27 point of view of the work which the dealer does. There
28 are, of course, foreign and central banks and I infer
29 that anything the dealers do -- and we certainly see
30 examples of fully hedged operations -- and other



1 people may employ the special deficits that they have
2 over here.

3 MR. HUNTER: At the moment the rate has been
4 moved forward to about $2\frac{1}{4}$ per cent per annum, which
5 takes any initiative away from the Americans; it is
6 too wide to let them profitably invest.

7 MR. HUNTER: The effect on commercial paper
8 would be about $3\frac{1}{4}$.

9 COMMISSIONER GIBSON: You mean that it is
10 encouraging the forward market?

11 MR. MILNER: Very definitely.

12 COMMISSIONER GIBSON: Are these large in
13 your opinion, Mr. Harris?

14 MR. HARRIS: No, but they do cause a
15 psychological effect to know that the market is going
16 out, and the treasury board and the market I think
17 on the whole are not ---

18 COMMISSIONER GIBSON: What sort of size is this?

19 MR. HARRIS: I did some research as far as I
20 could into the amounts that the dealers are involved
21 in in the New York banks, basically the New York
22 banks, and I see in March of this year it looked like
23 approximately 350 million were in these various types
24 of investments. Now, the bills of sale on short loans,
25 fully hedged loans in one year ---

26 COMMISSIONER GIBSON: This was money into
27 Canada from the States?

28 MR. HARRIS: Yes, but it is just through the
29 dealer operations; I have no idea how much will come
30 in through the chartered banks that deal through New



1 York and elsewhere.

2 COMMISSIONER GIBSON: That is a pretty sizeable
3 figure at one time.

4 MR. HARRIS: That was in March. At times it
5 is over 500 million.

6 COMMISSIONER GIBSON: Coming in?

7 MR. HARRIS: That you have here fully hedged.

8 COMMISSIONER GIBSON: You say there is money
9 that has moved the other way recently; is this the
10 same kind of size?

11 MR. HARRIS: No, I don't think so although one
12 has heard of quite good sized transactions but what it
13 will amount to I don't know. This comes up a bit
14 in papers payable by the chartered banks and other
15 depositors where money is in the chartered banks, but
16 most of this goes to the Canadian banks in terms of
17 U.S. dollar deposits and the figure is of a substantial
18 size. I think it would be above 100 million. I think
19 in Canada it would be about 150 million, but this is
20 the case.

21 COMMISSIONER GIBSON: This is highly valuable?

22 MR. HARRIS: Yes.

23 COMMISSIONER GIBSON: Therefore in a shorter
24 period I take it it could be very significant in the
25 market?

26 MR. HARRIS: Definitely because it can -- when
27 Canadian money goes out it takes it away from the
28 various banks and corporations and other people who
29 have to pay higher rates and it creates more interest
30 because of this.



1 COMMISSIONER GIBSON: Then you would, I take
2 it, in talking about the spreads on interest rates
3 between the two countries, and particularly in the
4 short-term field, attach great importance to the future
5 exchange market?

6 MR. HARRIS: Very definitely.

7 COMMISSIONER GIBSON: Do you consider this a
8 subject that ought to engage the attention of the
9 central bank?

10 MR. HARRIS: I think more than it does. I
11 think quite a few of the dealers are in contact with
12 the central bank and they know what is going on from
13 day to day. Our firm and other firms telephone them
14 in confidence, and they do know what is happening,
15 and I think it is important this relationship be continued
16 and that they are in close contact with what takes
17 place.

18 COMMISSIONER GIBSON: Do you see this kind of
19 business staying about the same, or growing, or what?

20 MR. HARRIS: I think growing. The dealers
21 have been quite active in advising and talking to
22 American corporations and American banks, and there
23 is the cost of the fully hedged short-term investments
24 and the interest rate differential, and this has grown
25 rapidly in the last three or four years and I think it
26 is an expanding operation. Another thing coming in
27 is that the Canadian accounts are becoming more educated
28 to putting money outside the country. At these higher
29 rates it is very worthwhile to put money overseas into
30 EURO-dollars.



1 COMMISSIONER GIBSON: Are these transactions
2 sensitive to very small differences in rate?

3 MR. HARRIS: Yes.

4 COMMISSIONER GIBSON: You people make it
5 your business to see they are -- or, some of the
6 investment dealer firms?

7 MR. HARRIS: Certain investment firms follow
8 this closely and one can move funds over to Europe
9 very quickly. With Telex and the rest of it, it is
10 a very sensitive and fast moving operation, and it has
11 been growing.

12 COMMISSIONER GIBSON: Are there many firms
13 engaged in this business in a serious way?

14 MR. HARRIS: No. I think they are growing
15 all the time. It is a very marginal profit. It does
16 lead to other business. You don't lose money, but you
17 don't make very much; but it has a lot of indirect
18 benefits.

19 COMMISSIONER GIBSON: Would they be mostly
20 the larger national firms in this?

21 MR. HARRIS: Yes, only five firms or so that
22 are actively in the overseas markets, but a number do
23 sell in the United States.

24 COMMISSIONER GIBSON: And that would be much
25 the bigger part?

26 MR. HARRIS: Yes.

27 MR. WADDS: There is nothing sentimental about
28 short-term money. We don't worry about the B.C.
29 Electric or anything. It goes where the rate is best.

30 COMMISSIONER GIBSON: That leads to the question



1 of longer term money and spreads. In B.51 you make
2 reference to the proper spread:

3 "Basically, the interest rates in the
4 United States and in Canada bear a definite
5 relationship and since we in Canada operate
6 in the dollar area, there is a substantial flow
7 of capital between the two countries. This
8 flow has the effect of arbitrage and tends
9 to have what is regarded as a proper yield
10 spread between the two markets, taking into account
11 the yield obtainable in the comparable credits
12 of the two markets and the level of our dollar
13 in relation to the United States dollar."

14 Would you elaborate on the question of a proper
15 yield spread? I take it you are talking about longer
16 term bonds, are you -- securities?

17 MR. ELY: This is the one that I wrote,
18 Mr. Gibson. There is a normal spread -- there has been
19 over the years. When our dollar was at the same level
20 as the American dollar, a half of one per cent spread
21 between comparable securities seemed to be recognized
22 as a normal spread between the two countries, and when
23 those spreads widened or narrowed money flowed each
24 way. When our dollar went to a premium you would
25 expect that spread to widen.

26 COMMISSIONER GIBSON: Why -- on the grounds
27 that the expectations would be that it would be go
28 back to par?

29 MR. ELY: That is right, and when our dollar
30 goes to a discount you would expect them to narrow.



1 COMMISSIONER GIBSON: For the same reason in
2 reverse?

3 MR. ELY; That is exactly right, and that is
4 the normal; but in the last few years, and more
5 important in the last year, the normal has not existed
6 because of the climate and the investor attitude towards
7 this country. So that now you have rather a reverse
8 situation where, comparing long-term United States
9 Governments with Canadian Governments you have one
10 and a half per cent in yield differential not even
11 taking into account the deep discount at which our
12 dollar is selling, and that should normally invite
13 a tremendous inflow of capital to this country with
14 the consequent narrowing of the spread. The opposite
15 is happening because of the attitude of the American
16 investor towards this country.

17 COMMISSIONER GIBSON: So we are getting what
18 you describe as a perverse reaction?

19 MR. ELY: That is right.

20 COMMISSIONER GIBSON: Why should people expect,
21 in the United States particularly, as a long-term
22 expectation that our dollar should be at par? Your
23 reasoning is based on that to quite a degree?

24 MR. ELY; Yes.

25 COMMISSIONER GIBSON: Do you think this is
26 a fact, that they do so expect -- that they have such
27 expectations?

28 MR. ELY: I think they do so expect. I don't know
29 whether you can put your finger on the basic reasoning
30 except that they are both dollars. Historically they move



1 either side, but there have been periods of premiums
2 and discounts that sort of centres the thinking of
3 their having some kind of a comparable value.

4 COMMISSIONER GIBSON: But now you feel that
5 the Americans have got over this fixation, do you?

6 MR. ELY: The market indicates it.

7 COMMISSIONER GIBSON: In other words, what you
8 are saying is that if things were as they should be,
9 the spread at present exchange rates would be a narrow
10 one -- half of one per cent or less?

11 MR. ELY: If the American investor -- and
12 that is the man we are talking about, putting his
13 money in this country -- if his view was that our
14 country was being run properly he would come in in
15 very big volume at these levels, but he has not.

16 COMMISSIONER GIBSON: Do you think there is
17 a danger that he may change his mind one of these days
18 and send in more money than we want to receive again?

19 MR. ELY: There is. There is a very definite
20 danger. It won't be apparent to most people when it
21 starts. If the policies which have been recently adopted
22 start to work and we conduct ourselves in such a way
23 that we repay or start to repay the short-term credits
24 which we have been given, there could start a very big
25 flow of money from the States to Canada.

26 COMMISSIONER GIBSON: And maybe you would be
27 in favour of government deficits at that point?

28 MR. ELY: No, I am never in favour of government
29 deficits. I think we all agree, and we have agreed in
30 this brief, that there are times for deficits and



1 surpluses. What we do not agree with was that during
2 the last few years we should incur deficits which built
3 our debt up from some 15 billion to 19 billion. This
4 is far too great, and the investor in foreign countries
5 is telling us that by not putting his money in and,
6 in fact, drawing it out.

7 MR. MILNER: I think I might add, I think our
8 central bank here is rather fearful of a permanent
9 fixed exchange rate just for the reason Mr. Ely points
10 out. In the 10 or 12 or 20-year period, whenever
11 the date was that we unfroze the dollar or put it on
12 a floating basis, the rate of premium was what cut
13 the American money coming here -- the unwanted American
14 money. After all, we are living with a country to the
15 south of us 10 or 15 times our size, and the movement
16 of funds from the United States to Canada can be very
17 detrimental to our economy if it becomes too great
18 or too little, and with the floating rate it was far
19 easier to regulate that flow. As Mr. Ely points out,
20 if this economy or austerity programme works here now,
21 I quite agree we could have a very large flow, an
22 embarrassingly large flow of American money into this
23 country with a fixed exchange rate. Whether the exchange
24 rate could be adjusted to take care of it I would not
25 care to comment.

26 MR. ELY: It could start very active dealing
27 in the forward exchange rate to slow it down if we see
28 it coming too fast.

29 COMMISSIONER GIBSON: This must put some of
30 you gentlemen in a very difficult position in advising



1 clients -- U.S. clients, and Canadian clients with
2 U.S. funds. What would you say today in these circumstances?
3 The picture as you present it is highly favourable for
4 moving American dollars into Canadian long-term securities.

5 MR. ELY: As far as rates are concerned?

6 COMMISSIONER GIBSON: Yes, all the mechanical
7 calculations suggest it is very good.

8 MR. ELY; That is right.

9 COMMISSIONER GIBSON: You must have a lot of
10 trouble in making up your minds about what sort of
11 advice to give.

12 MR. ELY: To American investors?

13 COMMISSIONER GIBSON: Or to Canadians who
14 own American funds.

15 MR. COX: I would agree with that.

16 COMMISSIONER GIBSON: Because, in effect,
17 you have got to assess this American opinion, or external
18 opinion of Canada against a statistical opinion?

19 MR. MILNER: But surely, Mr. Gibson, it is
20 too early yet to see whether -- I think your foreign
21 investor quite naturally today said, "Let us wait for
22 six or seven months" -- or whatever period of time he
23 wants, to see how this new programme might work in
24 Canada.

25 COMMISSIONER GIBSON: I am not expressing a
26 view. I am asking for yours.

27 MR. ELY: Statistically we should be
28 recommending to foreign investors that they put their
29 money in this country, basically looking at the exchange
30 rate and the differential in rates -- and we are trying



1 to do that all the time -- but they appear reluctant
2 because of other factors.

3 COMMISSIONER GIBSON: One day when and as this
4 programme takes it will all start swinging the other
5 way?

6 MR. ELY: We could have a very embarrassing
7 flow, and that is the time they will probably have to
8 change the level of the peg or maybe free it to stop
9 it before it gets too embarrassing.

10 COMMISSIONER GIBSON: As we did in 1950?

11 MR. ELY: That is right.

12 COMMISSIONER BROWN: Or operate on surpluses
13 and have very little interest. We realize this brief
14 was prepared by committees and therefore there will
15 from time to time be differences of opinion come up,
16 and Mr. Ely just commented on what he has written in
17 this respect in B.51. I wonder if we could have
18 the author of F.30 comment on his statement that it
19 does not seem likely that any regular spread in rates
20 between the two markets can be established.

21 MR. HUNTER: If you refer to pages 15 and 16
22 we have graphs there showing differential through the
23 years 1959, 1960, 1961 and part of 1962 on comparable
24 short-term U.S. and Canadian bonds, and in the long-term
25 area you can see where the spread widens out: In one
26 area as much as 1.71 and back to $1\frac{1}{2}$. Recently it has
27 been down about 80 basis points, prior to two months;
28 about 80 basis points. I agree with what Mr. Ely
29 says, that 50 basis points used to be regarded as the
30 normal spread but that really has not existed for some



1 years now, and I think that there are so many psychological
2 factors that enter into what the American investor does
3 and thinks -- his own market, whether the rates are
4 good there without coming into Canada -- and , as I said
5 earlier, the stability of our exchange rate for a
6 given period -- it is probably a very practical thing..
7 Most of the investors in Canadian securities are
8 institutional company people. They do not like to
9 make an investment today and find the rate changes 2
10 per cent by the time they report to their board.

11 COMMISSIONER BROWN: But your point is that
12 this stability, looking at the chart on page 16 --
13 the changes that occurred after this chart was made
14 when the spread suddenly widened from about 85 ---

15 MR. HUNTER: To 1.50 again.

16 COMMISSIONER BROWN: Yes, that this crisis
17 with respect to the foreign investors' attitude towards
18 the Canadian market has occurred only in the last three
19 or four months?

20 MR. HUNTER: You mean his desire to buy
21 Canadian securities?

22 COMMISSIONER BROWN: The crisis that has caused
23 the widening. If you expand the graphs to the last
24 two months, it is much wider.

25 MR. HUNTER: I don't think the American
26 investor has anything to do with it. In this instance
27 the American market has held fairly constant, and the
28 Canadian market has adjusted itself because of austerity
29 measures. In the meantime the American investor has
30 been sitting on the sidelines until in the last few days



1 there has been some indication he is taking an interest
2 again.

3 MR. COX: I think that half of one per cent
4 Mr. Ely refers to is the outgrowth of the fact Canada
5 financed its war effort at 3 per cent and the United
6 States at $2\frac{1}{2}$.

7 COMMISSIONER GIBSON: But the spread here, as
8 Mr. Ely emphasized, I take it is not just a spread in
9 interest rates. It is the expectation of lower exchange
10 rates as well.

11 MR. HUNTER: The exchange rate is really the
12 important thing. Why do the Americans think our dollar
13 is going to be at par with theirs? It has happened.
14 Anybody that has bought a security in the last 20
15 years has had an opportunity to get out at par, and
16 psychologically he thinks this is going to happen again
17 some day. Maybe he is right.

18 MR. MILNER: There is one point which might be
19 brought out at this moment. This goes back to withholding
20 taxes. Rightly or wrongly the American investor who is
21 fully taxable -- in other words, take a pension fund
22 type of investor, where they are tax free in their own
23 country: There is no rate of exchange at which they
24 will buy Canadian securities with a withholding tax,
25 because they argue that whatever rate they buy it at
26 is 15 per cent wrong because they are paying a premium
27 for something they don't get.

28

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1 And that is a very big factor to contend with. If
2 the withholding tax were completely removed you would
3 open up a very, very large old field of money that
4 would flow into this country.

5 COMMISSIONER BROWN: Is this a factor in
6 the long term Canada market?

7 MR. MILNER: In both.

8 COMMISSIONER BROWN: Most of the long
9 term Canadas were issued prior to December 20th?

10 MR. MILNER: The purchasing of some or
11 the re-investment of some funds has been completely
12 stopped or practically completely stopped by just
13 that peculiar factor.

14 MR. WADDS: I would say this, too, it
15 is a bigger factor in provincials than otherwise.
16 This is a trade secret I am letting out.

17 MR. HUNTER: We have not had a new Canada
18 long term issue for such a long time that I really do
19 not know what the true rate on long term Canadas is
20 at the moment. It is somewhat artificial due
21 to the activities of the purchase prices, et cetera.
22 There have been lots of sellers but few buyers. If
23 we have an issue of Canadas on long term probably we
24 will get down to some realistic knowledge on what
25 it should be.

26 MR. ELY: There is another factor that
27 comes into the picture. The state pension fund
28 in the United States amounts to \$36 billion and they
29 are normally buyers of Canadian securities. Since
30 they are subject to the 15 per cent withholding tax



1 they have not been buyers. That should make a tremendous
2 difference in inflow from that area alone.

3 COMMISSIONER GIBSON: The other question I
4 wanted to raise about the spreads was the point we
5 were getting along into, the spread between Canadian
6 federal and United States federal bonds and long term
7 corporate bonds. I understand if you do this the
8 spread is a little closer than it is in long term
9 governments or has been up until recently, is that
10 correct?

11 MR. COX: Yes, I believe it is. I
12 have been keeping track of yield spreads on double
13 and triple A utilities in the United States on things
14 like, say, Ontario Hydros and the spread has been
15 a little narrow.

16 COMMISSIONER GIBSON: This is some real
17 comparison because there is a big market on both
18 sides of the border?

19 MR. COX: It is a field in which the
20 American buyer is interested. He prefers our
21 Ontario Hydros to some high grade utilities in his
22 own market.

23 COMMISSIONER LEMAN: Mr. Gibson, I would
24 like to get one point clarified here. You are
25 not suggesting that the 15 per cent withholding tax
26 on Canadian pay issues held by non-residents be re-
27 moved, are you?

28 MR. WADDS: Yes, we are suggesting that
29 all withholding tax on Canadian securities be removed.

30 COMMISSIONER LEMAN: We have not had that



1 for years.

2 MR. WADDS: Yes, we had it on Canadian
3 government bonds. We had a 5 per cent tax on provincials,
4 15 per cent on corporates.

5 MR. MILNER: Actually, Mr. Leman, I think
6 the way, the solution to the withholding tax is to
7 revise the whole subject and that is what we are sub-
8 mitting in our brief. There are some rather peculiar
9 analogies in that withholding tax. Probably the right
10 thing to do would be to start afresh. It comes under
11 the tax agreement between the two countries. We had
12 up until December of last year external payment Canadian
13 bonds free of withholding tax.

14 COMMISSIONER LEMAN: That is what I wanted
15 to get straight. On U.S. pay bonds that is a different
16 matter. On Canadian pay bonds I could not understand
17 what your recommendation was.

18 MR. WADDS: The chief point we are trying
19 to get at here is to put a withholding tax on any
20 Canadian serviced external or internal bond you are
21 affecting the flow of American dollars in the long run
22 out of this country and if we are interested in financing
23 our debt then these impediments to free movement of
24 capital into this type of debt should be removed.

25 COMMISSIONER LEMAN: But if you buy a U.S.
26 pay bond in the States you would have 15 per cent
27 withheld against you?

28 MR. WADDS: That is right.

29 MR. HUNTER: I think it is more desirable
30 even on some internal Canadian securities in the United



1 States than it is on external securities. It takes
2 the responsibility for the exchange away from the
3 borrower and the interest payments et cetera are
4 not then subject to fluctuations of the Canadian
5 dollar.

6 MR. WADDS: A municipality that can
7 finance through Canadian pay securities and sell it
8 in the United States has developed no exchange
9 liability for itself and this can be very onerous
10 in certain cases. They are to certain municipalities
11 that have borrowed in United States dollars.

12 COMMISSIONER BROWN: One point I would
13 like to clarify and that is: Is it not correct on
14 a long term bond that was issued prior to the re-
15 establishment of the 15 per cent withholding tax
16 December 20th, 1960, for example, that conversion
17 has been free, that there is no withholding tax on
18 those even now?

19 MR. SHAW: The exemption from the with-
20 holding tax still applies.

21 MR. COX: I wanted to clarify this point --

22 MR. HUNTER: This is still a psychological
23 barrier as even those free of tax they do not like
24 paying tax to a foreign government and therefore they
25 sort of frown on our whole operation.

26 COMMISSIONER BROWN: Even though there is
27 no tax on those particular ones?

28 MR. HUNTER: Even though there is no tax
29 on those particular ones.

30 COMMISSIONER BROWN: There is a psychological



1 condition, is there?

2 MR. WADDS: That is precisely it.

3 COMMISSIONER BROWN: Let us take it up
4 psychologically.

5 COMMISSIONER MACKINTOSH: It seems to me
6 one thing is being sort of submerged here in the dis-
7 cussion on taxes. It apparently was the view in
8 imposing withholding taxes that we did not need this
9 American capital. All representations here seem to
10 be that we do need inflow of American capital.

11 MR. SHAW: We are fairly consistent in
12 that view. We did not share the concern that was
13 not so apparent for a while.

14 COMMISSIONER MACKINTOSH: I think we are
15 getting to a point where it ought to be brought out.

16 MR. MILNER: But, Dr. Mackintosh, the
17 reasons, I believe, for changing withholding tax
18 or deleting the advantages of withholding tax were
19 put on to discourage -- they were not put on to
20 discourage investment to the extent that they were
21 put on to effect the exchange rate when the government
22 at the same time made the announcement they intended
23 to depreciate the Canadian dollar from a premium.

24 COMMISSIONER MACKINTOSH: What was supporting
25 the Canadian dollar?

26 MR. MILNER: The flow of funds.

27 COMMISSIONER MACKINTOSH: Well, I take it
28 I am entitled to think then they wished to discourage
29 the inflow of funds?

30 MR. MILNER: They succeeded admirably.



1 COMMISSIONER MACKINTOSH: The point I want
2 to make clear is that you people say the flow of
3 funds to the United States cannot possibly end.

4 MR. HARRIS: Actually in December 1960
5 for the previous quarter, at that time there was
6 not a net inflow, it was pretty well averaged because
7 of repayment of insurance securities. This was not --
8 because of the concern that had been built up in the
9 press and various speeches, this was not really con-
10 sidered as serious as it should have been at the time.
11 The statistics were there but this was not a problem
12 actually in December of 1960.

13 COMMISSIONER MACKINTOSH: Well, in many
14 instances the government is a little late in getting
15 around to it.

16 COMMISSIONER LEMAN: Just one little
17 point following on this. We are talking about various
18 times here. At this time forget about the deficit
19 that Canada is still running. Is the level of
20 investment here in Canada that we do need external
21 capital to finance it?

22 MR. SHAW: The demand for investment funds
23 is made up both of need for investment capital and
24 need for money to finance deficits; in other words,
25 the demand for investment funds is very heavy in
26 Canada.

27 COMMISSIONER LEMAN: What I would like
28 to understand more clearly is whether what you would
29 be aiming for now is to get back the funds that have
30 flowed out over the period?



1 MR. SHAW: That is the first step.

2 COMMISSIONER LEMAN: And beyond that?

3 MR. MILNER: Well, Mr. Leman, this con-
4 versation has all been confined in relation to the
5 federal situation only. You have to add to that that
6 not only has the federal government spent a lot of
7 money but all governments in Canada spend a lot of
8 money. Provincial borrowings have been fantastically
9 high over the past ten or fifteen years and it really
10 goes down right into the municipal level. So when
11 you look at the payment problem or the interest
12 in having outside capital it is not only at the
13 federal government level; it is at all levels of
14 government that need capital and I think it would be
15 fair to say that if we are going to keep on at the
16 present rate of governmentals' spending that we will
17 need outside capital/^{in order}to procure the funds.

18 MR. ELY: I think what you asked, Commissioner
19 Ely, the first and most pressing problem is to conduct
20 ourselves in such a way that we regain our recent losses
21 and put the exchange fund back to the position it was
22 in where we have a proper level of reserves. Beyond
23 that we will certainly need money in this country if
24 we continue to expand. I would not think, referring
25 to a question that Mr. Gibson asked quite a bit
26 earlier, we would not need it in the same volume
27 that it was coming in in the 1950's.

28 COMMISSIONER GIBSON: I would like to
29 return to this question of the spread. I am sorry
30 to be so insistent but when we talk about United States



1 government and Canadian government spread, I think
2 it was said that the utilities spread was more
3 important in recent times and I wondered if you could
4 give us some idea how big this spread has been recently
5 between securities of which there is a volume?

6 MR. BEATTY: 1.65 per cent at the moment.

7 COMMISSIONER GIBSON: That would be between
8 what?

9 MR. BEATTY: Between the most recent high
10 grade utilities that were sold at tender in the
11 United States and the recent Quebec issue.

12 COMMISSIONER GIBSON: What is a reasonable
13 spread there? Would you take your one-half of one
14 per cent, Mr. Beatty, as being a sort of normal?

15 MR. ELY: No, on balance you might take
16 it maybe narrower than one-half of one per cent, the
17 dollar being at a discount.

18 COMMISSIONER GIBSON: Supposing the dollar
19 is at par -- one-half of one per cent?

20 MR. ELY: It used to be one-half. I would
21 think it would be wider than one-half now because
22 of the investment attitude of the foreign investor.

23 MR. COX: I think it has been in the range
24 of 80 cents to \$1.

25 COMMISSIONER GIBSON: My impression has
26 been three-quarters.

27 MR. MILNER: Three-quarters is about the
28 figure I would have given, Mr. Gibson.

29 COMMISSIONER GIBSON: So that the spread
30 there has actually been narrower than from looking at



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1 these charts?

2 MR. MILNER: Yes.

3 THE CHAIRMAN: Adjourn for ten minutes.

4 (At this point a short recess was taken.)

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1 THE CHAIRMAN: We will now resume.

2 COMMISSIONER BROWN: In section B, paragraph
3 8, there is a reference to inflationary tendencies.
4 I would just like to ask you for your opinion as to
5 the present force of these inflationary tendencies.

6 MR. ELY: In that section, Mr. Brown, I
7 was really referring to what had happened and, having
8 happened, why there were certain attitudes taken towards
9 long term bonds. I think the inflationary forces
10 are not in the economy today at all.

11 Do you want any further comment in that
12 regard?

13 COMMISSIONER BROWN: No, that is what we
14 wanted because there was the implication that unless
15 they are checked this investment direction was going
16 to continue to decline.

17 MR. ELY: I think they have checked them-
18 selves.

19 COMMISSIONER BROWN: What do you think of
20 the future?

21 MR. ELY: Well, inflationary forces in a
22 country turn investors to other types of securities,
23 obviously, than fixed income securities.

24 In the foreseeable future I do not think
25 there is much danger in this area, but we should
26 always be watching for it.

27 MR. COX: Mr. Brown, I have here a copy
28 of a brief that was presented by the Association be-
29 fore the Senate hearings on inflation. I do not
30 know if the Commission would like to have it or not.



1 It is quite authentic because one of the authors was
2 the Secretary of the Commission.

3 COMMISSIONER GIBSON: Is it up to date
4 reflecting your present views?

5 COMMISSIONER LEMAN: If so, it is probably
6 available to the Commission.

7 MR. SHAW: Perhaps.

8 COMMISSIONER GIBSON: To go to a new area --
9 now in respect of monetary policy and debt management,
10 your second recommendation suggests that we consider
11 separation of the control of the currency from debt
12 management. You say: that the Commission examine
13 areas of conflict between debt management and control
14 of currency with a view to determining whether these
15 functions should be separated.

16 We live with a sort of permanent problem
17 of trying to reach workable compromises between the
18 interests of debt management and the interests of
19 monetary policy. Your presentation brings this out
20 very clearly, because in section B, paragraph 14 you
21 suggest that debt management has been unduly subordinated
22 to monetary policy at times, and in section C, paragraph
23 8, you say that monetary policy is in fact being pushed
24 around by debt management.

25 I am not reproaching you for this apparent
26 conflict because I do not think it is a conflict. I
27 think this is in the nature of things; that debt manage-
28 ment and monetary policy are always trying to work out
29 reasonable compromises between the basic objectives,
30



1 and that this is more or less in the nature of control
2 in any modern society. You later suggest that debt
3 management should become directly under the control
4 of the Department of Finance. Would you elaborate
5 on this as to how you think it will help to solve
6 co-ordination of debt management policy and monetary
7 policy?

8 MR. MILNER: Mr. Gibson, before answering
9 that I might bring to the Commission's attention
10 that we have divergencies of views among ourselves
11 as to the right approach to this thing. I am going
12 to ask Mr. Ely, if I may, to start this, and Mr. Cox
13 to comment on it later.

14 MR. ELY: Mr. Gibson, you are talking
15 about paragraphs 14 and 15 in Section B?

16 COMMISSIONER GIBSON: Right.

17 MR. ELY: If you go to the latter part
18 of paragraph 15 of section B you will note that I say:
19 if that management were taken back to the Department
20 of Finance it would have the effect of bringing the
21 Department of Finance and the Cabinet into closer
22 association with the problems of raising money in
23 the capital markets to implement government fiscal
24 policies, which do not now adequately seem to reflect
25 the requirements of sound judgment.

26 I think in this particular portion of the
27 brief the whole approach was to get the problem closer
28 to the people who were creating it so there would be
29 a greater understanding of the problem of raising
30 money.



1 COMMISSIONER GIBSON: By doing this, of course,
2 you take the problem further away from the body
3 responsible for monetary policy. You still have
4 the problem of coordinating monetary policy and debt
5 management. How would you meet that?

6 MR. ELY: I think it would be met more
7 or less in the same way that it is met now, because
8 the Bank of Canada would be the advisor and there
9 would have to be complete and close collaboration
10 between the Bank of Canada and the finance department.
11 We understand that that is going on now in a pretty
12 satisfactory manner.

13 COMMISSIONER GIBSON: If the Bank of Canada
14 is the advisor, will it also be the operator?

15 MR. ELY: I think the Department of Finance
16 might even ask the Bank of Canada to be the operator
17 until they can staff the Department of Finance with
18 the kind of people who can handle it. There is
19 very close collaboration between the two, and there
20 should be, but the fundamental approach is still that
21 if you take it to the Department of Finance you then
22 bring it closer to the people who are creating the
23 problem.

24 COMMISSIONER GIBSON: But you still have
25 to have coordination?

26 MR. ELY: Always.

27 COMMISSIONER GIBSON: And are you going
28 to have two groups of people operating the security
29 market with ultimately the bank on the one hand the
30 Department of Finance on the other?



1 MR. ELY: I think eventually you can
2 only have one group operating it so that you leave
3 then the Bank of Canada in charge of monetary policy
4 and the Department of Finance in charge of debt
5 management in its entirety.

6 COMMISSIONER GIBSON: But then you get
7 the two inextricably muddled up at the security
8 purchase and selling level, and the one effects the
9 other, in other words?

10 MR. ELY: That is right. I think that
11 on the secondary marketing operation, rather than
12 the primary operation, it would have to be carried
13 on by the bank, but when it came to the primary
14 operations they would be conducted by the Finance
15 Department.

16 COMMISSIONER GIBSON: The primary operations;
17 you mean quotations on new issues and refundings?

18 MR. ELY: New issues and refundings.

19 MR. MILNER: I would like to have Mr. Cox
20 speak on this as well.

21 MR. COX: I think the feelings in section C
22 were similar to those expressed by Mr. Ely. We have
23 a comparison which perhaps is not necessarily valid
24 because situations are different from one country to
25 another. We have in the United States a federal
26 reserve operating the monetary policy and we have
27 the treasury doing debt management. It seems to work
28 relatively well.

29 I think there is also the aspect that the
30 Bank of Canada is now being asked to do too much. If



1 the bank were in a position to devote itself to a
2 greater extent to monetary policy problems, and the
3 Cabinet were made more aware of the difficulties that
4 their fiscal policy might create on the capital markets,
5 this might be a step in the right direction.

6 COMMISSIONER GIBSON: Yes, but the problem
7 that I do not quite understand is that you are going
8 to have two people operating in the security market
9 more or less parallel to each other, are you? Is it
10 your thinking that by having what you might call an
11 investment department within the Department of Finance,
12 with the added skills and abilities there, it would be
13 beneficial to the operation of both debt management
14 and monetary policy?

15 MR. COX: Yes, I believe that. I think
16 you also have to bring in fiscal policy. Debt manage-
17 ment arises in many instances, or the province of
18 debt management arises from fiscal policy.

19 COMMISSIONER GIBSON: Yes, but you see
20 the Bank of Canada now is the agent of the Department
21 of Finance in debt management.

22 MR. COX: Yes.

23 COMMISSIONER GIBSON: Unless you build
24 up an operating department in the Department of Finance
25 there really is not much difference between the situation
26 that exists now and what would exist in the future.

27 MR. COX: I think we envisage a complete
28 department as they had prior to the Bank of Canada
29 to look after debt management in the Department of
30 Finance.



1 COMMISSIONER GIBSON: And how do you get co-
2 ordination between the two investment organizations?

3 MR. COX: By liaison of the very highest
4 degree, of course.

5 COMMISSIONER GIBSON: You do not think it
6 is better to have one investment department with the
7 finance department than in the position to state what
8 policy is now in debt management? It is its basic
9 responsibility.

10 MR. WADDS: There is no question as to
11 whether that would result over a period of time.

12 COMMISSIONER GIBSON: This is, you say,
13 the underlying constitutional effect?

14 MR. WADDS: Yes.

15 MR. MILNER: Under existing circumstances
16 in the last few years there have been many instances
17 where the central bank has been running both ways
18 at the same time. It has been operating for the
19 debt management in one term and from a banking view-
20 point as the central bank in another viewpoint. They
21 are converse; completely different objectives in
22 both cases. We had in mind that if you reverted
23 to the pre Bank of Canada situation where the Department
24 of Finance was responsible for debt management and the
25 Bank of Canada responsible for monetary policy you
26 would not have that conflict, and you would have a
27 much clearer picture before the public. We are not
28 unanimous at all in this view and possibly the fault
29 might be remedied in another way. Unfortunately
30 what has happened in the past number of years is that



1 the Bank of Canada has become sellers of securities,
2 let us say, not for their own account, but for the
3 government account, but the general public has not
4 been aware of who they were selling for, and before
5 we knew it we had a situation where we had a rising
6 or falling market caused by a cause which was not
7 correct. It was not monetary policy, it was merely
8 that they were selling for a government fund.

9 COMMISSIONER GIBSON: But you see, you
10 approach this problem, and I have it in mind even
11 more, by saying that the bank is trying to go in
12 two directions at the same time. How do you get
13 around that? Putting debt management under the
14 Department of Finance does not avoid this basic
15 conflict. If considerations of that management
16 are to do one thing and monetary policy to do another,
17 there is still the conflict. It still has to be
18 resolved. Somebody has to work it out. I think
19 if you propose this sort of thing you ought to show
20 how these conflicts can be worked out. Liaison is
21 one thing but how do you get this liaison? The
22 Department of Finance is now in a position to state
23 what the policy is in respect to debt management.

24 MR.MILNER: Mr. Cox, would you like to
25 go on in that regard?

26 MR. COX: I think it gets back to the question
27 that the department is looking after debt management.
28 Its influence with the government is going to be
29 considerably greater in the department's fiscal policy.

30 COMMISSIONER GIBSON: You are really saying,



1 if the Department of Finance were closer to this their
2 fiscal policy might be affected in what you would
3 regard as a constructive way, is that right?

4 MR. COX: Yes.

5 MR. ELY: That is correct.

6 COMMISSIONER GIBSON: I do not think you
7 have answered the question as to how you would do this
8 in an operative way. You cannot escape these con-
9 flicts; they are inherent in our society.

10 MR. COX: But we hope the conflicts will
11 be less dangerous and there will be greater harmony
12 between the three items of fiscal policy, debt management
13 and monetary policy.

14 COMMISSIONER GIBSON: Mr. Milner, you say
15 you do not all agree on this subject. Would some
16 of the people who do not agree care to say something?

17 MR. MILNER: Just as you are saying, Mr.
18 Gibson, some of us feel it is almost impossible to
19 separate the two and have them operating. I think
20 Mr. Harris has got something he might wish to say in
21 this regard.

22 MR. HARRIS: I tend to agree with Mr. Gibson,
23 I think.

24 COMMISSIONER GIBSON: I have not expressed
25 a view.

26 MR. HARRIS: Well, you expressed it
27 perhaps indirectly. We have had pretty unusual times
28 during the central bank history in this country. We
29 have had unusual circumstances within the bank and
30 within the government. In the long run I think you



1 would be creating a problem by putting it in two places.
2 You may create more political problems possibly in the
3 long run. I think at the moment it may be attractive
4 from our point of view where we have lacked direction.
5 We have found it, as dealers, a difficult thing under
6 certain conditions. I can see more problems over
7 a longer period perhaps if things were split in this
8 way.

9 Surely the bank is, as you say, the advisor
10 and agent of the Department of Finance. Perhaps
11 one problem is that the Department of Finance until
12 fairly recently has not taken as active a role as it
13 should have in looking at the capital markets. It
14 has not had the people. I think this has been corrected.
15 They are taking a more active role in studying markets
16 and studying the effect of issues upon the markets.
17 This has perhaps been the problem in the past. I
18 think it is improving now. I think it is fully aware
19 of this problem and taking a much more active role
20 in policy.

21 MR. ELY: Mr. Gibson, I was one who was
22 not completely in accord although we held a discussion
23 last night and I think we tried to resolve our
24 differences.

25 The reason I was not in accord was
26 that I felt that taking debt management out of a non-
27 political body and putting it into a quasi-political
28 body might possibly mean that it would be run along
29 more political lines which would be wrong in our opinion.
30 I wanted to separate the political approach by leaving



1 the whole thing with the Bank of Canada as a non-
2 political operating body.

3 We felt that the argument was outweighed
4 on the side of getting the problem closer to the
5 people who created it.

6 COMMISSIONER LEMAN: You would not suggest
7 that the government should go and ask the bank how
8 much money it will let it have to carry out policy?

9 MR. ELY: The government is all powerful
10 and when the chips are down it tells the bank how
11 much money it wants, there is no asking.

12 COMMISSIONER MACKINTOSH: This is a point
13 I think we ought to clarify. The present arrangement
14 is that the Minister of Finance is the principal and
15 the Bank of Canada is the agent.

16 MR. ELY: That is right, sir.

17 COMMISSIONER MACKINTOSH: My understanding
18 is that the Bank of Canada always makes clear in its
19 transactions whether it is acting as agent or acting
20 as principal on its own account. I do not know how
21 the public gets this confused view that they are
22 acting in different ways, but I should think the
23 only information the public had would come later
24 when the accounts come in. Certainly it does not
25 show up in the Bank of Canada accounts in respect
26 to unemployment insurance, but that would show up
27 in the unemployment insurance fund later.

28 MR. SHAW: The difficulty, Mr. Mackintosh,
29 is that we are talking about the public. I think
30 we were referring to our traders and people who are



1 clearing on day to day transactions, and the bank
2 does not tell us why they are doing these things.

3 It is left to us to infer what is behind these
4 purchases or sales. Sometimes we are led to
5 the wrong conclusion in talking to the same fellow
6 on the telephone when he is selling or buying, and
7 we attach a significance to it which is incorrect.
8 He is not doing it from a monetary policy point of
9 view, he is doing it because he has instructions
10 as an agent to carry out some particular job.

11 COMMISSIONER MACKINTOSH: My understanding
12 is that he tells you he is acting in one capacity
13 or the other.

14 MR. SHAW: Unfortunately he does not, sir.

15 MR. ELY: He does not tell us.

16 MR. MILNER: Mr. Harris may wish to answer
17 that.

18 MR. HARRIS: I think very often there are
19 occasions when they state they are acting on an account,
20 but I believe there are many times when transactions
21 are done and they are reluctant to indicate that. It
22 may be that a trader in Toronto or Montreal does not
23 really know at the time.

24 COMMISSIONER LEMAN: Perhaps he should ask
25 if he is not told.



1 MR. HUNTER: I mean, the bank trader has
2 to be told by Ottawa.

3 COMMISSIONER MACKINTOSH: Is this a continuing
4 variation in procedure? Our understanding is that
5 there are traders who are always informed.

6 MR. MILNER: There is probably no one ---

7 COMMISSIONER MACKINTOSH: Your experience
8 is that they are not?

9 MR. HUNTER: I do not think there is an
10 active trader here, but it is my understanding that
11 we are frequently at sea whether it is for monetary
12 policy or against.

13 MR. MILNER: Would you like to answer
14 that, Mr. Cox?

15 MR. COX: Our troubles have been told
16 on occasion, but I would not like to leave the impression
17 they say they are acting for an account.

18 COMMISSIONER MACKINTOSH: You say they do
19 not invariably say it?

20 MR. COX: Very definitely they do not
21 invariably, contrary to what their brief suggests.

22 COMMISSIONER BROWN: They also confirm
23 the ticket and it makes it quite clear they are acting
24 for another account. Of course, you do not get that?

25 MR. COX: No, and I do not know that very
26 many of us see the tickets.

27 MR. SHAW: It would be far better to do so --
28 the method of operation, is it not true, is that the
29 only way we can find out what the bank is doing is to
30 go to them and they very, very rarely initiate an interest.



1 Am I right in that, if you want to find out what the
2 bank is doing you try them out on a bid and they accept
3 it or not.

4 COMMISSIONER MACKINTOSH: Is not that the
5 way you usually find out how the market is doing?

6 MR. SHAW: That is right, but in the
7 circumstances is it not quite possible there would
8 be no further conversation and then you try them out
9 with another block and see how far they are prepared
10 to go. It is a fair trade operation without too
11 much conversation as to why the operation.

12 MR. HUNTER: One of the problems is that
13 the Bank of Canada is the major factor on the market
14 and every known bond trader or institution that deals
15 actively in securities will take no action, even in
16 the provincials or other securities, he wants to know
17 what the Bank of Canada is going to do, and this is
18 such a focal point that if a dealer thinks that the
19 bank is meeting a certain price for bonds they will
20 offer bonds to find out if it is. If not, they
21 will offer them down, which starts a deluge of selling
22 which might not have occurred if the bank had not
23 been in the picture at all.

24 COMMISSIONER GIBSON: To change the subject
25 for the moment; another very important statement in
26 section C, paragraph 28, is the statement which comes
27 out in favour of the "preferably" policy for the
28 Bank of Canada open market operation. The Association
29 does not make this recommendation although it is
30 contained in Section C; the view is expressed it is



1 desirable in Section C. Would you care to comment on
2 that?

3 MR. COX: Well, you accept the concept
4 that when the bank wants to buy securities they want
5 to deal with the reserve of the chartered banks and
6 it can be done just as effectively in a treasury bill
7 and it can be done with less destruction of the market
8 because it is done under the shorter term segment than
9 under the longer term segment and you get higher points
10 in yield -- I think it is one cent in price and one-
11 half a point on a twenty year bond, and if you
12 operate in the long segment of the market you are
13 liable to create an artificial level, which has several
14 weakening effects on the strength of the actual level
15 where the market should be. I am not expressing
16 this very well.

17 COMMISSIONER GIBSON: I think you are
18 making your point reasonably clear.

19 MR. COX: And the best digest
20 I have seen on this subject is by Winfield Riefler,
21 published in the 1958 Federal Reserve Book and there
22 are several quotes in one of the paragraphs here in
23 Section C.

24 COMMISSIONER GIBSON: But you make this --
25 I would not say "recommendation" -- about the bills
26 of the short market operation and the Association
27 does not recommend this. Do you disagree on this
28 point or is the Association in agreement with Mr.
29 Cox's view or the statement given in Section C.

30 MR. ELY: I think, Mr. Gibson, that you
must recognize that there are 197 members of the



1 Association and there are only 14 money market dealers
2 who have any real knowledge of this subject, and even
3 amongst the 14 money market dealers there might be
4 only a percentage of them who would be experts, so
5 it would be very difficult to get the broad agreement
6 of the Association on something that involves only
7 a very few houses.

8 COMMISSIONER GIBSON: This is the reason
9 you have not given it as an Association recommendation;
10 not that you disagree, but it would take people who
11 are experts.

12 MR. ELY: That is right. At our session
13 at Lucerne on this subject we are talking about there
14 were really very few people who had any views on it
15 at all.

16 COMMISSIONER GIBSON: It is not out of
17 harmony with some of the banks' views. Perhaps you
18 might refer to the central bank's brief, Mr. Cox; I
19 glanced over it and they said they are in favour of
20 that policy in general. Are there any comments you
21 would like to make?

22 MR. COX: We suggest there are occasions
23 when it might be helpful for the central banks to
24 operate on a longer term basis. This would be
25 on the conditions that the market becomes disorderly
26 or ----

27 COMMISSIONER GIBSON: You are not finding
28 disorder!

29 MR. COX: It is very difficult to trade,
30 and where trades tend to take place at considerable



1 changes in price and there is little continuity
2 to it and the volume has declined because of the
3 difficulty with trading, and it would be opposite
4 to the broad resilient type of market that is con-
5 sidered desirable.

6 COMMISSIONER GIBSON: You believe there
7 are circumstances such as the very recent one where
8 the central bank should be in the market?

9 MR. COX: I think they should be stabilizing
10 to some extent; not necessarily ordering the direction
11 of the trend of the market, but stabilizing it so
12 that some trade can take place, and this is something
13 that is very well dealt with in several federal reserve
14 conflicts and they have a similar view in the States
15 that a disorderly market should not be allowed to exist
16 because it creates a great deal of apprehension and
17 since the government market is the central point around
18 which all other interest rates fluctuate, it effects
19 all other types of credit and all other types of
20 borrowing.

21 COMMISSIONER MACKINTOSH: Should they "pre-
22 pare a good reception" for the issue?

23 MR. COX: I think they have been known to.

24 MR. HUNTER: The Bank of Canada has been
25 using this purchase fund operation to help stabilize
26 the market for the past several weeks and it has
27 eased things down a bit.

28 COMMISSIONER GIBSON: So when the variations
29 become large the spreads become wide; that is the
30



1 case that the central banks make out?

2 MR. COX: I think we should keep the appre-
3 hension at a minimum rather than emphasizing it.

4 COMMISSIONER GIBSON: I hear from what
5 you might call die-hard individuals who say they
6 would rather not have a long market in any circumstances;
7 if everybody knew they were not there at all you would
8 get a better market ultimately. Is there anything in
9 that?

10 MR. HUNTER: Yes, I think there is something
11 in that; this disorderly thing is ---

12 COMMISSIONER GIBSON: You would have to put
13 it with disorder if you accepted that?

14 MR. HUNTER: You would have to, yes, but
15 I think this is sufficiently important because the
16 effects of rapid changes in yields of Canadian bonds
17 affects yields of other securities to quite a con-
18 siderable extent.

19 As a matter of fact, there are some figures
20 here which I might leave with you. In the past two
21 years, from June 1960 to June 1962 there have been
22 six important changes in the direction of the yields,
23 and despite the fact that there was only one long -- it
24 was actually a C.N.R. issue in the fall of 1960, and
25 since then there has not been any long issues at all.
26 The total change on yields in that period -- and this
27 is based upon an average of yields for each month --
28 the total change on yields on Canadian is 1.67 per
29 cent, whereas on provincials -- where there has been
30 a tremendous amount of operating change -- it is only



1 1.46 per cent. In other words, Canada is 15 per cent
2 more than the provincials, although the government
3 has refrained from operating in that field.

4 COMMISSIONER GIBSON: How does this bear
5 on the business deals, only occasional intervention?

6 MR.HUNTER: I think it is the fact they
7 have been intervening in the long market that caused
8 these wider fluctuations.

9 COMMISSIONER GIBSON: Is it not a fact
10 that this has had something to do with their being
11 able to support the market in recent years?

12 MR. HUNTER: Well yes, I think that has
13 been their endeavour; whether they have succeeded in
14 doing this is a question that might be debated.

15 COMMISSIONER GIBSON: But you are almost
16 saying that the fact that they are known to be inter-
17 vening at times is a disturbing element on the market.

18 MR. HUNTER: It becomes -- I do not know
19 that these price levels are exactly right because
20 I am working from memory here, but the purchase fund
21 was at 83 earlier this year and the market is in the
22 range of 91 and 92, and the market then moved up to
23 the 94 range, and as far as we know the bank did not
24 raise its purchase fund until they all of a sudden
25 moved it up two points and got it up to the trading
26 level of the market again. Then it went down, and
27 maybe the bank actually had an instruction from the
28 Department of Finance to take so many bonds at 94,
29 and they took them, and then had to keep shooting it
30



1 down the market as fast as they could.

2 COMMISSIONER GIBSON: Your other members
3 more or less agree with the view that there are times
4 when the Bank of Canada should enter the market?

5 MR. MILNER: The Bank of Canada entered
6 the long term market in a very large way and the fact
7 of the Bank of Canada owning such a tremendous amount
8 of long term debt, in our opinion, has had a very
9 deterring effect on the long term Canada market ever
10 since because you always have the overhanging view-
11 point that if the market were to go up it could absorb
12 a huge amount of the Bank of Canada's holdings and that
13 the Bank of Canada would love to be rid of their debt
14 and operate as a bank in the immediate and short
15 term fields, so that this is where we have disagreement
16 amongst ourselves. There have been suggestions,
17 for instance, which were made -- it was considered
18 as a suggestion that the Bank of Canada might freeze
19 its long term Canada position to get rid of the
20 fact that that was always overhanging the market
21 and if there were no long term securities held by
22 the Bank of Canada -- not the government of Canada
23 but the Bank of Canada -- I think we would have a
24 much more realistic open market in long term investment;
25 I think it would be a much broader margin than exists
26 today.

27 COMMISSIONER GIBSON: You are not altogether
28 agreeing with Mr. Cox; he said there were circumstances
29 when the Bank of Canada should prevent disorderly
30



1 conditions, and you think it would be better if they
2 did not intervene at all in the long market?

3 MR. MILNER: I think, Mr. Gibson, that
4 my conception of disorderly conditions might be
5 different from some of the other committee, but my
6 conception of a disorderly condition applies both
7 ways; you can have a disorderly market going up as
8 well as one going down and there have been two or
9 three occasions when we have had a disorderly market
10 on the reverse end; that is, too quick a rise ---

11 COMMISSIONER MACKINTOSH: You want them
12 to intervene on both sides?

13 MR. MILNER: I think the function of the
14 Bank of Canada -- this is my personal view -- I think
15 the function of the Bank of Canada primarily is to
16 attempt to stop excess movements of markets which
17 are not in accordance with governmental policy, and
18 that would apply both ways.

19 MR. COX: If you want it to apply both
20 ways. I used the example of the declining market.

21 COMMISSIONER GIBSON: This raises all kinds
22 of problems because you say you are in favour of bills
23 preferably, but if the conditions are disorderly in
24 either direction it may mean that the central bank
25 should intervene. I do not know how you can define
26 "disorderly" in this sort of way.

27 MR. HUNTER: Maybe the advantage to having
28 a Canadian market is that it could be the Department
29 of Finance who intervenes in a disorderly market.
30



1 COMMISSIONER GIBSON: This gets back to the
2 conflict between management and the policy -- if they
3 are doing something which is in conflict with the Bank
4 of Canada, it is still being done and has to be co-
5 ordinated.

6 MR. HUNTER: I think the action of the Bank
7 of Canada in the recent applications has been largely
8 on behalf of the Federal government for a purchase
9 fund. I do not think that the Bank of Canada is in
10 the wrong end of the market -- at least, I do not know.

11 COMMISSIONER BROWN: They have been buyers
12 and not sellers.

13 MR. HUNTER: We have been sellers recently,
14 but we do not know.

15 COMMISSIONER GIBSON: Let us put it another
16 way. We have a modern type of free enterprise
17 society and in this kind of society the dealer has
18 to carry a fair load. Should you give the authorities
19 the responsibility of sustaining the bond market
20 or, indeed, from preventing it from going up too high
21 with very strong pressures the other way; you are in
22 effect trying to moderate the changes in existing
23 rates that occur from time to time and which are part
24 of the machinery for trying to check the boom or
25 stimulate the recovery. Do you want to moderate
26 the changes?
27
28
29
30



1 MR. MILNER: We want to smooth out the excessive
2 movements either on the upside or the downside. My
3 conception of the way, for instance, the exchange fund
4 operated over the past five years was trying to smooth
5 out -- they didn't try to force a rate either way.
6 They merely prevented it from going too far either on
7 the up or the down side, as the case may be, too quickly.
8 On the governmental long-term bond market you have got
9 an exactly similar situation, that if the dealers,
10 which is our industry, misjudge a market to the extent
11 of driving prices up too fast by accumulating a huge
12 inventory position, it is probably not in the best
13 monetary interests or fiscal interests of the country,
14 and it is very easily stopped by the Bank of Canada,
15 either on the government account or its own account,
16 moderating that upswing. But the main objection, I
17 think I am right in saying, we have had over the past
18 five or six years has been that on the downswings we
19 rather question whether the bank's efforts on the
20 downswings were as effeciently carried out as they
21 might have been. The bank has always had a tendency
22 to support a market to a point and suddenly withdraw
23 support. Instead of having supported the thing on
24 a gradual basis on the way down they have simply with-
25 drawn support, and you get excess drops in government
26 securities because of that particular action.

27 COMMISSIONER GIBSON: Now you are talking
28 about the efficacy or the efficiency of their operations.

29 MR. MILNER: Yes.

30 COMMISSIONER GIBSON: I was trying to get you



1 more on whether they should intervene or not and under
2 what circumstances? Let us assume the operations are
3 efficient.

4 COMMISSIONER BROWN: There is one question
5 while we are on this: First of all, we will go back
6 a little on this question of bills preferably policy.
7 It was explained because there were only 14 members
8 of the I.D.A. in this market that as an association
9 they could not express a view, but for the record,
10 could we have some expression as to the degree of
11 unanimity among the 14 members of the money market?

12 MR. MILNER: Yes. On the 14 money market
13 dealers I would think we would be unanimously in favour
14 of the operation.

15 COMMISSIONER BROWN: I just wanted to get that
16 on the record because it was not clear.

17 MR. MILNER: We have here today about 6 of
18 the money market dealers.

19 MR. HARRIS: I think in reading the Bank of
20 Canada's brief there are statements one cannot disagree
21 with where they say:

22 "In carrying out open market operations
23 to provide or withdraw cash reserves the
24 Bank of Canada usually, though not always,
25 chooses to deal in relatively short-term
26 securities in order to minimize the direct
27 impact of its transactions on the market."

28 I think we all agree with this in theory,
29 but, as Mr. Hunter has said, the theory does not
30 quite follow because we don't know quite what is



happening, and if we always knew there were offerings for monetary policy in the short end I think it would be better. I think it reads very well, but in practice it does not quite follow. Again they say:

"... and letting the responses of banks and others to this change work themselves out in the markets ..."

It sounds quite good, but at times there are little mechanical things which upset it: Markets are not the same for one dealer as another.

COMMISSIONER BROWN: These are the techniques; we will get into that later. I wanted to get the principle.

MR. MILNER: You asked the question, and I would say that the money market dealers would recommend Section C.28.

COMMISSIONER BROWN: The next question is that if the Bank of Canada is operating on the short end of the market for the purpose of monetary policy this is obviously going to have a reflection on the long end: How fast do you think this effect should go?

MR. WADDS: Sometimes it does not seem to affect the rest of the market too much. We have seen many occasions in recent years where traditional yield curves have completely vanished. We have had reverse curves.

COMMISSIONER BROWN: Why has this occurred?

MR. WADDS: That is a good question. I would like somebody else to answer that.

MR. BEATTY: This seems to occur when the



1 yield on long-term government bonds becomes so
2 attractive to a wide range of investors that they
3 become eager to take advantage of it.

4 COMMISSIONER GIBSON: They then do not respond
5 much to change in the short end?

6 MR. BEATTY: That is right.

7 MR. MILNER: Not too much. In recent years,
8 even for the last two years -- let us not bother
9 about the last two weeks; I am thinking about a normal
10 market: You could have a rise or fall in the short-term
11 market of five basis points without having any effect
12 on the long-term market. That would be correct, Mr.
13 Hunter?

14 MR. HUNTER: Yes.

15 COMMISSIONER BROWN: Your suggestion is that
16 if it is going through to the long end of the market
17 the Bank of Canada should smooth it out so it does not
18 affect the long-term so quickly?

19 MR. HUNTER: We may be forgetting one instrument
20 that has not been used for a long time: The bank rate,
21 itself. It is going to have an influence if the monetary
22 authorities felt the thing was getting out of hand,
23 and a bank rate adjustment might temper the psychology
24 of the buyers.

25 COMMISSIONER BROWN: I agree with that, but
26 what we are trying to deal with at the moment is the
27 question of the bills preferably. What I am trying
28 to get at is an expression of opinion as to what you
29 expect the Bank of Canada to do or not to do in the
30 long end of the market if the monetary policy is going



1 to become effective through operating in the short end.

2 MR. ELY: I think the Bank of Canada has to
3 operate in the long-term market from time to time in
4 a smoothing operation so that there is some continuity
5 following through from what they are doing in the
6 short market.

7 COMMISSIONER BROWN: What I want is the expression
8 of opinion as to how they should operate in this smoothing
9 operation. Say, through their operations in the short
10 market the short-term goes up?

11 MR. ELY: To carry out monetary policy?

12 COMMISSIONER BROWN: Yes.

13 MR. ELY: Yes.

14 COMMISSIONER BROWN: Is it your conception
15 that they should only gradually increase the rates
16 or operate so that the rates in the long end change
17 only gradually?

18 MR. ELY: I think that is right.

19 COMMISSIONER BROWN: In other words, this gives
20 fast movers the opportunity to move before other people?

21 MR. MILNER: But a smoothing out operation.

22 MR. ELY: I hadn't thought of it in that light.
23 What I was thinking about was, if the Bank of Canada
24 are carrying out on behalf of the government a monetary
25 policy and operating in the short end of the market --
26 say, on bills only -- then, there should be some relation
27 between that end of the market and the long end of it,
28 and they should endeavour to do the smoothing operation
29 in the end not so certain fast operators can buy or
30 sell them at levels that may not exist some time later,



1 but so there is a minimum fluctuation in the top security
2 in the country and confidence is retained in the reason-
3 able changes that take place rather than violent
4 changes.

5 COMMISSIONER BROWN: This all comes into the
6 question of the speed with which people get the message
7 that there are going to be higher interest rates, and
8 if everybody gets the message that the interest rate
9 is going to change at 5 cents throughout, and therefore
10 the long bonds are going to come down half a point --
11 I am just asking whether you think this half a point
12 should come down in eighths or by half a point.

13 MR. ELY: It is a difficult question to answer,
14 but the smoother the operation the less disturbance
15 to the vast number of people who own the bonds always --
16 who are pure investors.

17 COMMISSIONER BROWN: If it is going to come
18 down half a point, anyway, this means that some people
19 are going to get down just one-eighth, and the faster
20 this market operates ---

21 MR. ELY: The faster the change takes place
22 the less opportunity ...

23 COMMISSIONER BROWN: ... for competent operators
24 in the market to get out before ---

25 MR. ELY: Yes, I see that. I was taking another
26 view, because certainly some of the confidence that has
27 been shaken, some of the investor confidence that has
28 been shaken has been shaken because of the wide
29 fluctuation in the top security of the country, and
30 one would hope that fluctuation could be mitigated by



1 a smoothing operation, whether it is one-eighth, three-
2 eighths or a quarter, is the view I was taking. It is
3 a question of smoothing.

4 COMMISSIONER GIBSON: You are really suggesting
5 that the central bank should have a view about yield
6 curves at any given time. What I would like to ask
7 you, is the same kind of yield curve always appropriate?

8 MR. ELY: No.

9 COMMISSIONER GIBSON: Are there times when
10 short yields should be relatively high and long yields
11 relatively low, and so on? If this is the case, what
12 does the central bank do?

13 MR. ELY: I think the central bank should always
14 have a view of what kind of a yield curve is appropriate
15 to carry out monetary policy, and there would be times
16 when yields on shorts should be greater than those on
17 longs and vice versa.

18 COMMISSIONER GIBSON: But you are going a long
19 way from the idea of bills preferably.

20 MR. ELY: I didn't say I was married to the
21 fact they can only be on bills preferably.

22 COMMISSIONER MACKINTOSH: You didn't say you
23 were divorced.

24 MR. ELY: There are times when these things
25 cannot be too rigid. The Bank of Canada say the need
26 to co-ordinate central bank operations with government
27 debt management operations is another reason why the
28 Bank of Canada feels it should not rigidly restrict
29 its dealings only in the short-term securities. I think
30 that right: It should not be rigid; there must be some



1 leeway.

2 COMMISSIONER GIBSON: You think most of the
3 time it should not be in the long-term market at all?

4 MR. ELY: I think it should always have a
5 watching brief on the long-term market, but perhaps
6 one could say they should not be in it to the extent
7 they are from time to time.

8 COMMISSIONER MacKEEN: It has been suggested
9 that the Bank of Canada should intervene in the long
10 market to relieve a disorderly condition. I think it
11 would be helpful to us if you gave us your ideas at
12 what stage an orderly market became a disorderly market?

13 MR. MILNER: Mr. MacKeen, that is quite a
14 question. A disorderly market, if you take my first
15 saying where it is either up or down, the central bank
16 by operating in the long-term market during that period
17 when it either became a rising or falling market, just
18 using a hypothetical theory -- say, they had \$10 million
19 worth of bonds they were prepared to play with. Over
20 the course of a year or so they would buy and sell this
21 \$10 million worth of bonds possibly 25 times. Each
22 time they were doing it would merely be to stop the
23 market going up by half of one per cent or half a point
24 in 15 minutes or going down a point in 15 minutes.
25 They would simply use that fund as a levelling influence
26 to stop these very wide swings either way, but they would
27 not eventually accumulate a higher or lower inventory.
28 COMMISSIONER MacKEEN: Would you say it would
29 become a disorderly market when on the down side you
30 could not get a bid at a reasonable price?



1 COMMISSIONER BROWN: What is a reasonable price?

2 COMMISSIONER MacKEEN: Something within the
3 range of what the market had been.

4 MR. MILNER: Well, government markets should
5 not vary by one per cent overnight in yield -- or,
6 one per cent in price. That is a very wide swing,
7 in our opinion -- to have a market change by one point
8 in one day. There are times, such as we have gone
9 through recently, when that might have been impossible,
10 but under the normal spread in a normal market of
11 government bonds, I think I am right in saying if you
12 had a half a point spread at the maximum would be the
13 normal spread that should exist.

14 COMMISSIONER MacKEEN: And still be in the
15 orderly market.

16 MR. MILNER: Yes.

17 COMMISSIONER MacKEEN: Marketing range?

18 MR. MILNER: Yes.

19 COMMISSIONER BROWN: If the street anticipated
20 this was going further, how much would they have to
21 absorb in any one day? This is part of the problem,
22 isn't it?

23 MR. ELY: A disorderly market -- usually when
24 we talk about disorderly markets we talk about markets
25 that are going down. The reason I bring up this point
26 is that disorder is caused by forced selling, and a
27 disorderly market is caused when dealers, who are
28 merchants just the same as a department store, have
29 inventory on their shelves for their customers who
30 because of the precipitous drop in the market are forced



1 maybe by the bank from whom they are borrowing the
2 money to finance that inventory. to sell.

3 COMMISSIONER LEMAN: You don't use Government
4 of Canada shorts as loss leaders?

5 MR. ELY: Another case of a disorderly market
6 would be when the brakes on the chartered banks are
7 put on too hard so they are literally forced to sell
8 securities to keep their reserves at a proper level --
9 maybe forced too quickly and in too great volume,
10 far greater volume than the market will take, so you
11 get disorder. Disorder is when owners of securities
12 are forced to sell.

13 COMMISSIONER GIBSON: Is disorder just the
14 suddenness of the change or the degree of the change,
15 because I would suggest to you at times if the central
16 bank's desire was to really tighten the rein and
17 affect bank lending policies as well as investment
18 policies that quite a significant change in interest
19 rates may be required?

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1 And therefore you might be able to avoid a substantial
2 change; in other words, are you just objecting to
3 the suddenness of it or the amount?

4 MR. ELY: I am objecting really to the sudden-
5 ness of it and the degree. Better foresight might
6 mitigate the suddenness and the degree.

7 COMMISSIONER BROWN: We have heard in all
8 our hearings expressed many times the desire for clearer
9 signals of what the central bank is trying to accomplish.

10 MR. ELY: Yes.

11 COMMISSIONER BROWN: And it seems to me that
12 the clearer the signal -- at least I will reverse that,
13 I would like to get your reaction to the suggestion
14 that the clearer the signal the more violent the
15 reaction.

16 MR. ELY: I think that is quite right.

17 MR. SHAW: The sharper and more painful the
18 signal the more clear it becomes.

19 COMMISSIONER BROWN: You are putting the egg before
20 the chicken. If everybody gets a clear signal that we
21 are in for tighter money ---

22 MR. ELY: Then the sharpness is going to
23 be multiplied.

24 COMMISSIONER BROWN: Then you are almost in
25 favour of not such a clear signal?

26 MR. ELY: I think that with better planning
27 the condition could be brought about over perhaps a
28 longer period.

29 COMMISSIONER GIBSON: In a gradual way through
30 the market?



1 MR. ELY: In a gradual way through the
2 market than giving a signal which might cause speculation
3 in securities which are not deemed by the investor to
4 be speculative.

5 MR. MILNER: In other words, Mr. Gibson,
6 what Mr. Ely, I think, is saying is that if the bank
7 for proper reasons wanted to tighten the monetary
8 supply, the flow of funds, that by the time they had
9 tightened them sufficiently the market would have
10 moved prior to that point; in other words, they would
11 have gradually altered the interest rate so that there
12 was not a sudden violent change in one day's time.

13 COMMISSIONER GIBSON: What you are saying is
14 where you have enough foresight to avoid crises?

15 MR. MILNER: No, crises are a different thing
16 altogether. That is a thing that is almost impossible
17 to cope with but on normal business conditions.

18 COMMISSIONER GIBSON: To avoid disorderly
19 conditions on the market.

20 MR. MILNER: To avoid disorderly conditions.
21 Forgetting about this last month, in the last two or
22 three years there have been very marked changes in
23 interest rates, very wide swings in interest rates
24 that I would think could have been evened out to a much
25 greater degree than we have witnessed.

26 COMMISSIONER BROWN: How would this be
27 accomplished because there was no clear signal in
28 that period? They were all gradual and they became
29 clear as people knew what was happening.

30 MR. MILNER: I think that the central bank,



1 for instance, after they changed governors a year or
2 so ago, there was a pretty clear signal given that
3 the monetary policy was being altered and money would
4 become easier. This would take a certain amount of
5 time for that to get into the stream and it was then
6 tightened up at odd times here and there because they
7 had got too much money in it and I think in the last
8 year or year and a half that we have witnessed bank
9 signals and I think if you go to England, for instance,
10 or the American market usually what happens there is
11 that the bank rate is altered after the event is over.
12 The market activities would, owing to the fact that
13 money is becoming easier, there will be a drop in the
14 bank rate and should the drop occur it does not affect
15 their long-term or short-term market to any appreciable
16 extent.

17 COMMISSIONER LEMAN: I would like to get some-
18 thing a little more clear in my mind as to what is the
19 balance of your opinion on this matter. You said that
20 if the Bank of Canada as a matter of course stayed
21 out of the long-term market the market itself would
22 be broader and I presume you meant by that that it
23 would tend to be more orderly, does that follow?

24 MR. MILNER: Yes.

25 COMMISSIONER LEMAN: Are you in fact saying
26 the bank should adopt this policy and when the investment
27 dealers, those who are in the primary market for
28 securities, are unable to keep it orderly then the
29 bank should step in? Is it not reasonable to assume
30 that for someone to accept this sort of last resort job



1 to back up a market that has become disorderly,
2 it is much easier to do this if the primary agents
3 figure in their own minds how they will operate from
4 time to time to prevent disorderliness? It is hard
5 to accept this sort of last ditch job. You cannot
6 guarantee to the Bank of Canada that you can keep the
7 market orderly, can you?

8 MR. COX: No, we cannot control our customers.

9 COMMISSIONER LEMAN: I think a fellow, any
10 institution or agent is entitled to have the whole
11 job to do or nothing at all.

12 MR. WADDS: There is a pretty wide range
13 of opinion as to how much the Bank of Canada should
14 be in this long-term market. I do not think it should
15 be in it at all under any circumstances and then we
16 would have a market that would be at least realistic.
17 This is a personal opinion but I would far rather take
18 my chances with free market forces than dwell in the
19 field of uncertainty that we are in at the moment and
20 I think it is fairly general here, as shown by dealer
21 inventories, that there is a reluctance on the part
22 of most dealers to take long Canada bonds. At the
23 same time I think many of the dealers have taken very
24 substantial positions in long-term provincial bonds
25 which is a pretty free market. You can see this fact
26 by long Canadas to a certain extent but nevertheless
27 there has been more incentive to take positions in
28 long-term provincials than Canadas for some time.

29 MR. COX: You know central bank cannot use
30 provincial bonds to implement its monetary policy.



1 COMMISSIONER GIBSON: So you have a pretty
2 wide range of opinion on this, really.

3 COMMISSIONER BROWN: If the Bank of Canada
4 were out of the long-term bonds and there was this
5 change in the short-term Canadas would you change your
6 long-term markets?

7 MR. WADDS: Well, a free market is supply
8 and demand. I do not think we would significantly
9 change our long-term market. You take these long bonds
10 on the premise that you can sell them; it is not a
11 speculation.

12 COMMISSIONER GIBSON: You have to assess the
13 market and make up your mind?

14 MR. WADDS: Yes.

15 COMMISSIONER GIBSON: One other thing about
16 this business about the long operations by the Bank
17 of Canada that I would like your opinion on: Suppose
18 the country has an investment pool and there is more
19 capital investment going on than you have got resources
20 to handle, in other words, the situation brought about
21 by a big capital investment boom -- and we have had this
22 situation in Canada. Some people believe in those
23 circumstances that the central bank should deliberately
24 try to place the rate of interest, If so, if you
25 tell us you are not working the long-term market,
26 that may not work as well. Any thoughts on that?

27 MR. COX: They have got a whole set of tools
28 available to them and open operations is only one.
29 Could they not influence the trend of interest rates
30 by using some of their other tools?



1 COMMISSIONER GIBSON: I do not say this is
2 likely to happen often but it has happened when you
3 are in a position where you have a capital investment
4 boom which is excessive on its demands on the economy.

5 MR. COX: Like we had in 1955 and 1956?

6 COMMISSIONER GIBSON: Yes. What do you do?
7 Do you just work in short things then?

8 MR. COX: Won't the demand for capital change
9 interest rates by itself if the demand is greater than
10 the supply?

11 COMMISSIONER GIBSON: That is what I am asking
12 you.

13 MR. COX: Won't interest rates go higher without
14 central bank action?

15 COMMISSIONER GIBSON: It should but maybe
16 the central bank wants to give it a push.

17 MR. COX: I would think it would be appropriate
18 to think about using some of the other tools they have
19 at their disposal.

20 COMMISSIONER MACKINTOSH: I think the difference
21 between you and Mr. Ely is that he would nudge that yield
22 curve along.

23 MR. ELY: I think there is an essential difference
24 in our opinions here. I find it difficult to think that
25 they should not exert some influence in the long-term
26 market.

27 MR. SHAW: Perhaps I had better stand up and
28 be counted here. I would like to go back to the wording
29 in the brief and, speaking in a personal point of view
30 because even within one organization you will get



1 different points of view -- I think personally that
2 the Bank of Canada should operate strictly within the
3 bills preferably area, the exception being during
4 periods of crises rather than disorderly markets. We
5 have been trying to define disorderly markets and I
6 think Mr. MacKeen came as close to it as I might have
7 done that when you get no bid within a reasonable length
8 of when the last previous trades have taken place
9 or no offerings within the same limit you are in some
10 sort of a disorderly market. The dealers should
11 have the opportunity of contending with that in their
12 own way to the point where, if it gets completely out
13 of control then I think you get into a period of
14 crisis and at that stage the central bank, in my view,
15 should depart from the bills preferably concept. I
16 think the wording here would clear my position.

17 COMMISSIONER MacKEEN: Mr. Shaw you think
18 if the Bank of Canada had no long-term bonds they
19 could not do anything very much to halt a disorderly
20 upswing, could they?

21 MR. SHAW: They might like to do as we have
22 to do; they might have to borrow some from the dealers
23 who were short. If we found ourselves in that very
24 desirable position I would think the chances of a
25 crisis developing would be considerably less.

26 COMMISSIONER GIBSON: I think we have discussed
27 this question at a fair length. Could we go on to the
28 question of the term of the national debt. In Section
29 B, paragraph 35 you suggest that the term of the
30 national debt should be a bit longer in Canada than the



1 States because of the more open type of economy and
2 less developed markets. What do you think the average
3 term of the debt should be in Canada as a general
4 proposition?

5 MR. ELY: I have said, Mr. Gibson, that I
6 think it should be longer than in the States, the
7 reason being that in the States semi-government bodies
8 finance themselves in the long-term market whereas
9 in Canada government bodies are financed by the
10 government. Those same bodies that would be long-term
11 borrowers are financed directly by the government. I
12 do not know how you put your finger on exactly what
13 average term our debt should have but let me put it
14 this way, that the problems that have been created
15 in the American market by having the very short debt
16 are not insurmountable but they are close to it and
17 they have the problem of raising money coming at them
18 every few months and if that circle continues where
19 do they end?

20 Now, therefore, one assumes that the longer
21 your debt the easier the debt management becomes and
22 certainly for borrowing on the part of the government
23 in many cases money they borrow is for long-term
24 purposes. On balance I would say that the longer we
25 can keep the average term on our debt in this country
26 the better conditioned by the fact that they must have
27 at all times enough debt in the short-term sector
28 to control monetary policy.

29 COMMISSIONER GIBSON: Then, how do you go
30 about carrying out this objective of keeping the period



1 of debt as long as you can? You are suggesting that
2 when conditions are depressed there should be a good
3 deal of refunds and conversion of long returns?

4 MR. ELY: How do you go about it?

5 COMMISSIONER GIBSON: Yes, because when
6 conditions are depressed you want to get the stimulus
7 from monetary policy in terms of somewhat lower interest
8 rates and if you take advantage of that to refund a
9 good deal of debt to longer terms you may not pass
10 this benefit along to the private economy to the same
11 degree. In other words, there is something of a conflict
12 here between desire to convert the long-term and the
13 desire to stimulate the economy by lowering the
14 interest rates. What are your views on that?

15 MR. ELY: I see what you mean and I appreciate
16 it. The reason we have not been able to extend the
17 average term of our debt is a certain lack of confidence
18 in the securities involved. If that confidence returned
19 by proper management of our over-all policies there
20 would be a greater tendency on the part of Canadians
21 to buy the long-term debt and in that area it may be
22 reasonable to expect that there would be more stability
23 in the long-term market which is what the long-term
24 investor is looking for.

25 COMMISSIONER GIBSON: And the idea of stability
26 in the long-term market is the real motivation, in
27 your thought, that we do things in long terms in
28 periods when business is depressed and when there
29 is an upturn in business you would accentuate the rise
30 in long-term interest rates?



1 MR. ELY: That is right.

2 COMMISSIONER GIBSON: And this is really a
3 very interesting dilemma -- and it really is a dilemma --
4 between debt management and monetary reform?

5 MR. ELY: Yes.

6 COMMISSIONER GIBSON: Anyone else have any
7 views?

8 MR. MILNER: That is one of the things that is
9 right throughout our thinking, that that would be
10 one of the methods of stopping the greater fluctuation
11 in interest rates.

12 COMMISSIONER GIBSON: Don't you see lower.
13 interest rates sometimes and higher interest rates at
14 other times as useful tools of national economic policy?

15 MR. MILNER: Yes, but I do not think the very
16 wide spreads are as effective as more gradual changes
17 in interest policy. Following your line of thinking
18 we would never have as high a long-term market if
19 at times when we wanted to make money easier instead
20 of having our interest rates go to, say, 3 per cent
21 they would only go to, say, 4 per cent because there
22 would be a greater pressure on the longer term market.
23 We would not have nearly as wide swings as we have had.

24 COMMISSIONER GIBSON: But the question I am
25 really trying to get to is do you think the combination
26 monetary and fiscal policy could be effective if there
27 were not quite wide swings?

28 MR. MILNER: Those swings could be more
29 accentuated in the short-term and less in the long-term.

30 COMMISSIONER GIBSON: Really you are saying



1 you would like really more stability in this picture
2 than we have experienced in recent years. That is
3 a fair statement, is it?

4 MR. MILNER: Yes, that is a fair statement.

5 MR. ELY: We are really portraying the views
6 of the investor along that line.

7 MR. BEATTY: It has been used to a great extent
8 to combat business cycles.

9 COMMISSIONER LEMAN: But going back to the
10 matter of signalling, don't you think with this process
11 you might take as a signal the decision by the federal
12 government to lengthen the term of its debt at any
13 moment as an indication that in their view they have
14 about come to the peak of the market? Would it not
15 be interpreted as such?

16 COMMISSIONER BROWN: What would be the effect
17 on the market?

18 MR. BEATTY: It would tend to reduce the
19 extent of the swings.

20 MR. SHAW: Should not the federal government
21 be expected to take a somewhat different view there
22 than other credit such as provinces and municipalities
23 or corporations who understandably seek to float their
24 issues at the most favourable level of the market
25 to them whereas when dealing in the federal field and
26 you have many objectives, that the federal government
27 should not be so concerned with reaching the top of
28 the market for their financing? If they are right
29 in that objective or successful in that objective then
30 they sell their issues at the time and in the meantime
the public who own them are a discontented lot.



1 Their objectives are manifest although I
2 do not think the federal government should be quite
3 prepared to accept the difficulties involved in
4 operating long term issues perhaps at the higher
5 level of the market. This would satisfy that
6 and would achieve that objective of lengthening
7 out the debt, making your other tools in the monetary
8 policy field much more effective.

9 COMMISSIONER GIBSON: With the benefit
10 of hindsight on this whole question of term, would
11 you care to express an opinion about the effectiveness
12 of the conversion operation of 1958?

13 MR. SHAW: The effectiveness or the effect?

14 COMMISSIONER GIBSON: The effectiveness.

15 MR. SHAW: It is quite effective, I think,
16 in obtaining the objectives they set out to obtain.
17 It is a successful operation from the point of view
18 of the government to extend the term.

19 COMMISSIONER GIBSON: Yes, but looking
20 back on it?

21 MR. SHAW: Looking back on it now, the
22 cost may have outweighed the advantages to some extent.
23 I do not adhere to the view that it was an entirely
24 bad thing, but it did bring in some very unfortunate
25 developments.

26 MR. ELY: I think it is quite fair to say
27 here that at the stage when they were initially under-
28 way on the conversion loan there was very marked
29 deterioration in the American bond market to which
30 our market bears a relation, so that some of the



1 criticism, I think, should be mitigated if one looks
2 at what happened in a market right next door to ours
3 which we could not fight.

4 COMMISSIONER GIBSON: What I am really getting
5 at is, do you envisage that we are going to have to
6 do a job like this every five or six years to get
7 reasonably stable, and if so, what did we learn from
8 the last conversion?

9 MR. ELY: No, I do not think we have to
10 do a job like this every few years, Mr. Gibson.
11 I think it can be done gradually at the appropriate
12 levels, because with the stability which we ask
13 for and the same increase in confidence in the way
14 the country is being handled, there is a market for
15 long term securities. There is a sufficient market
16 for long term government securities to allow it to
17 issue long term securities.

18 MR. MILNER: The conversion, Mr. Gibson,
19 was too great for the size of our debt. The conversion
20 was too big. Had that been, whatever percentage
21 you want -- 15 or 25 per cent of what they bid --
22 there would not have been the repercussions that
23 occur. I am certain of that.

24 COMMISSIONER BROWN: You mean, in other
25 words, if they had not been so successful in their
26 operation it might have been better?

27 MR. MILNER: Yes, at the beginning it
28 was too big. We tried to do too much in one operation.
29 Of course, the handling of the after market in our
30 opinion was a tragedy.



1 COMMISSIONER GIBSON: Of course, there
2 was no escaping the fact that interest rates were
3 going to go up. They went up abroad.

4 MR. MILNER: Yes, they went up everywhere.

5 COMMISSIONER GIBSON: They went up here.
6 In your opinion did it accentuate the rise, or was
7 it about the same?

8 MR. MILNER: The chartered banks knew
9 very well what would happen. When the chartered banks
10 foresaw the change of interest rates the government
11 maintained its purchase funds at par until they
12 bought back a huge amount of bonds. That effect
13 would not have occurred had the government had an
14 orderly market, alternating their price until the
15 selling dried up. I do not know what the price
16 would have been, but it would not have gone from par
17 at the opening to around 96 or 97 in about one minute.

18 COMMISSIONER BROWN: They should have
19 gone down gradually?

20 MR. MILNER: They should have kept dropping
21 off until the selling dropped off, but by arbitrarily
22 setting a standard price with a sum of money involved
23 and just running out of the money and that was the
24 end, that was a bad thing.

25 MR. WADDS: This also occurred on the longer
26 end with the insurance companies; particularly in
27 relation to the long conversion bonds. They immediately
28 saw the changing interest rate and they unloaded them
29 as quickly as they could, so there was quite a lot
30 of pressure on the Bank of Canada.



1 COMMISSIONER BROWN: This was the point
2 that we were discussing earlier. The more people
3 that become sophisticated, the faster that happens
4 in any event. .

5 MR. WADDS: That was my original argu-
6 ment, Mr. Brown. If bonds start to disappear
7 the sellers stop selling. This is the practical
8 effect. They cannot sell and they will not sell
9 them scaled down.

10 COMMISSIONER GIBSON: Would you like
11 to talk about bank rates? In your recommendation
12 23 you suggest that the bank rate should be re-
13 established, but in recommendation 24 you also say
14 that the present system of a floating rate should
15 continue to apply in money market jobbers.

16 At the present time we have just about
17 this, of course; we have got a special announced
18 bank rate and a bank rate which is a quarter over
19 the treasury bill rate for money market jobbers.

20 In Section C, paragraph 43, it states
21 that the dual rate does not seem to make too much
22 sense if people do not borrow money at both rates.
23 Supposing you suggested that the chartered banks
24 borrow at 6 per cent and the money market dealers
25 at the other rate; what about this? Do you like
26 this change in securities from the point of view
27 you had in mind?

28 MR. MILNER: Here again we had differences
29 in our own viewpoints of the dual rate, but if I may
30



1 speak for a moment about the fixed bank rate I shall
2 do so.

3 I know that there is great difficulty in
4 a country such as Canada being so close in the North
5 American continent to the United States that a fixed
6 bank rate here is much more difficult for us than
7 for most normal countries. On the other hand, it
8 is overweighed, in my opinion, by the fact that I
9 think all over the world we have in all the so-called
10 free world where there are central banks, what is
11 known as the bank rate, the bank rate gives an
12 indication to outside people of the general monetary
13 conditions which necessitate the bank rate being
14 at whatever it happens to be at -- 3, 4 or 5 per cent.

15 We were practically unanimous in our view-
16 point that Canada over a long period of time would
17 be far better off with that fixed bank rate as an
18 indicated rate even though it is not used to the same
19 extent here as it is used in other countries with the
20 central banks.

21 When it came to the money market dealers,
22 this was in a rather difficult category. As you well
23 know, in the American market they have no such thing
24 as a double rate, but they have another method of
25 accomplishing the same thing. This is done by the
26 federal reserve being willing to purchase securities
27 from money market dealers with no obligation to purchase.
28 It is clearly a different type of purchase and resale.
29 We have a line of credit. The money market dealers
30



1 have obtained that line of credit, and we think that
2 the quarter penalty rate is a perfectly rational
3 situation compared to a similar situation in the
4 United States. We also came to disagreement among
5 ourselves as to whether two rates might defeat
6 the purpose of only having one rate. I think Mr.
7 Harris should start in this regard because he was
8 one of those very interested in this bank rate.

9 MR. HARRIS: I was looking at this
10 situation from the money market point of view.
11 First of all, speaking from a very selfish money
12 point of view, the variable rate fills a useful
13 function inasmuch as it irons out changes in availability
14 of day loans. We have to bank our inventory in that
15 day loan market. There have been operations of the
16 central bank contrary to chartered banks, which has
17 kept the cash requirements pretty strict over the
18 period of recent years. There were times when
19 money was not available so dealers had to go to the
20 Bank of Canada quite often, although the Wednesday
21 evening figures only show this as eleven weeks in
22 1961 for the total year. However, I think that
23 on many more occasions it happened other than
24 on Wednesday nights. The dealers, if they carry an
25 inventory, take a responsible role in making any
26 difference in the money market. Money market dealers
27 feel there is some accommodation available to them.
28 From a very selfish money market point of view we
29 feel we could be satisfied with this rate, and it is
30 recommended in the money section.



1 When you actually come to the two rate
2 system setup, the immediate problem is, would anybody
3 borrow at the 6 per cent rate; would the money market
4 dealers help the chartered banks out so that nobody
5 would be using the 6 per cent? If the Bank of Canada
6 took these steps and the dealers would not undertake
7 to help the chartered banks out during periods when
8 things were tight, this is a problem. I think this is
9 a necessary move to make this thing work. I am sure
10 that they would abide by that policy. If we have to
11 try to continue to keep that amount of money market
12 securities which are necessary in the development of
13 the money market, one needs to know where the source
14 of borrowing is.

15 At times in the past certainly when we
16 had a fixed bank rate there was a wide spread between
17 the bank rate -- in 1955 and early 1956 -- and the
18 money market rates. Since then I think the money
19 market has grown because the dealers have felt a little
20 more secure in holding money market securities.

21 From the money market point of view there
22 is an advantage in a flexible rate. There are certain
23 differences in this point of view.

24 MR. MILNER: Mr. Cox, would you like to
25 comment in this regard?

26 MR. COX: The point of view that I took was
27 that any hint or indication that there was a dual rate
28 took away from the effectiveness of the fixed administered
29 rate. I think that we all agreed that we wanted this
30



1 returned to a fixed rate because this is a signal that
2 indicates that a change in economic conditions are in
3 the offing or perhaps have already commenced to show up.

4 The point of view I took in respect to the
5 special lower rate to the money market dealers was
6 that if the bill rate dropped considerably lower than
7 the bank rate -- say that the bank rate was 6 per
8 cent now and the bill rate got under 5 -- somebody
9 is wrong. If the dealers are able to move their
10 bills at something under 5 per cent the Bank of Canada
11 monetary policy is not in keeping with its administered
12 rate level. On the other hand, if the dealers are
13 wrong in bidding bills up to something under 5 per
14 cent, I do not quite see why they should get a special
15 cushion for them. In the normal course of events in
16 our business if your judgment is wrong you pay the
17 penalty, and if your judgment is right you profit
18 from it.

19 I should like to say in passing also that
20 subject to the change in the bill level today the
21 dealers are now able to borrow at 5.68. You technically
22 borrow at 6 per cent but because you borrow at 7 and
23 only get credit for 5, when you are establishing your
24 cash ratio, I do not think it is unfair to say you
25 pay 6 plus 40 per cent which is 8.40.

26 I think that perhaps Mr. Rasminsky has
27 recognized the same difficulty in the weakness of his
28 position of having the dual rate by getting in touch
29 with the banks and dealers. I would not like to think
30 that we are going to leave this dual operation in force



1 too long, because this would enable the bank, if it
2 saw fit again, to get away from the fixed rate. They
3 hint in their submission to you that there are pros
4 and cons both in respect to a floating rate and a
5 fixed rate. I would think I would not like to see
6 them get away from the fixed rate.

7 COMMISSIONER GIBSON: In other words
8 you would like to see them, if it were possible, re-
9 turn to one fixed rate?

10 MR. COX: Yes.

11 COMMISSIONER GIBSON: What would you think
12 about a compromise idea; instead of having one-quarter
13 of one per cent of the treasury bill rate for the
14 floating rate to have a variable percentage above
15 the treasury bill rate depending on what the Bank
16 of Canada thought? If it thought money was getting
17 tighter it might make it one-half, or if it was
18 getting loose or easier, it might make it one-eighth.

19 MR. COX: That would still defeat the
20 effectiveness of the administered rate, in my idea.

21 COMMISSIONER GIBSON: I suggested that
22 instead of the other, Mr. Cox.

23 MR. COX: I would not like to see us get
24 away from the administered rate.

25 COMMISSIONER GIBSON: If you varied the
26 rate it would be a signal. It would be a conscious
27 act there for people to see.

28 MR. COX: Would it be as well understood?

29 COMMISSIONER GIBSON: I do not know.

30 MR. COX: Would it be as well understood



1 internationally as domestically?

2 COMMISSIONER GIBSON: It would be more
3 technical, that is clear. Would you say it would
4 be desirable in your opinion?

5 MR. COX: I think it would have some effect,
6 but I do not know that it would be quite as effective.

7 MR. WADDS: I do not think it would be
8 as effective as the floating rate which we have had,
9 which was virtually nil outside the country as well
10 as inside. This was the one thing we could look to
11 to give us some guidance.

12 COMMISSIONER GIBSON: But if the Bank of
13 Canada instead of saying that the bank rate is one-
14 quarter over the treasury bill rate, it said it is
15 one-half over the treasury bill rate, this is an
16 expression of opinion and not an automatic thing.

17 MR. WADDS: It is still affected by the
18 public tender, is it not?

19 COMMISSIONER BROWN: What do you think
20 the effect on public tender would be?

21 MR. WADDS: The only reason I say that,
22 Mr. Brown, is that it has happened over the years
23 and has been occurring on the bill market and it
24 always seemed to me that there was a strange thing
25 when we had a so-called fixed rate that could be
26 affected by the dealer or somebody blowing up the
27 bill rate. This is not a signal to anybody except
28 to those individuals who want to pay a lot of money
29 for bills.
30



1 MR. COX: There is one other thing involved
2 here. It is recognized by some that the central
3 bank policy could be more effective if they used
4 more than one tool; if they used the open market
5 policy to change the bank reserve, and they also
6 want to change the interest rate. If they change
7 the discount rate at the same time, probably the
8 open market operation could be less extensive
9 with less risk of creating disruption in the market.

10 COMMISSIONER GIBSON: Do I detect a
11 difference of opinion between you and Mr. Harris?
12 You would like to go back to the fixed rate and
13 drop the floating rate?

14 MR. COX: Yes.

15 COMMISSIONER GIBSON: And Mr. Harris, I
16 think, likes the dual system, is that fair?

17 MR. HARRIS: From the money market point
18 of view it is better. From the ^{strict} point of view of
19 the money market it plays a useful function.

20 COMMISSIONER GIBSON: This is part of the
21 consideration. Do you think the floating rate is
22 good from the money market point of view?

23 MR. HARRIS: Again going back to the problem
24 discussed before the recess, it floats back and forth.
25 We do have a problem in moving funds back and forth.
26 This is affected by the situation in the United States.
27 If you are going to have a bank rate that is fixed,
28 I think that it is indicated it has to be fixed for
29 a reasonable length of time and not as a result of
30



1 difficulties in the money market caused by changes
2 taking place between the two countries interchanging
3 short funds. Certainly from the money market point
4 of view there are difficulties involved.

5 As I say, there are other arguments. I
6 do not think the money market dealers disagree with
7 the other arguments at all, but there is this conflict.

8 COMMISSIONER GIBSON: What do you think
9 about the idea of changing this to a sort of floating
10 rate?

11 MR. HARRIS: I must say that it is a new
12 idea which I had not thought of before, or even heard
13 mentioned. On the whole I do not know whether it
14 would help. Perhaps it might to a certain degree.
15 I still feel this quarter of a point is a good working
16 figure for the money market. I think we are better
17 off with one or the other, but I do not think that would
18 really solve the problem. It would be another way of
19 avoiding certain responsibilities. I suggest this
20 would create delays in making the change. The Bank
21 of Canada again seems to feel here that the fixed bank
22 rate might be changed, but that the bank rate would
23 be delayed until it was more certain that a change
24 was indicated. This again brings up the other problem
25 of when to change it, and when to give the signal.

26 MR. MILNER: Mr. Ely, do you wish to say
27 something in regard to this subject?

28

29

30



1 MR. ELY: I was one of those who had
2 views that we should consider a dual rate. The reason
3 for having a different rate for many market dealers
4 than the fixed bank rate in my opinion was that if
5 bills were selling considerably below the administered
6 rate it would considerably inhibit the size of the
7 money market if dealers had to go into it at a penalty,
8 and the size and depth of the money market is an
9 important thing in this country. These are my
10 considerations in suggesting that they should hang on
11 to the quarter of one per cent above the average so that
12 there wouldn't be a large penalty at times which would
13 make hills and valleys in the broad concept of the
14 money market.

15 COMMISSIONER GIBSON: I am just trying it out.

16 MR. ELY: Your idea that from time to time
17 there might a change in that quarter of one per cent,
18 according to which way the income was going, I think
19 has a lot of merit; It is worth thinking about and
20 studying because it could act in a smoothing way with
21 regard to the money market.

22 MR. SHAW: Is it the case, Mr. Chairman, that
23 the spread between the money rate and the bank rate
24 of as much as one per cent necessarily means that
25 somebody is wrong? Is it not true that in England --
26 I have a chart in front of me here from the period
27 1952 to 1954 -- well into 1954 -- and the spread between
28 the treasury bill and the bank rate was 2 per cent
29 in favour -- the bank rate was at the higher level,
30 the bank rate was staying at 4 per cent, I think, and



1 the treasury rate was reaching between 2 and 1-3/4,
2 and isn't that sort of thing likely possible to happen
3 without necessarily one or the other being wrong?
4 We don't want to change too frequently; we have seen
5 occasions in the States where the bank rate has been
6 below the bill rate for some little time and the dealers
7 have been able to take some benefit from carrying this
8 on inventory for their own account.

9 COMMISSIONER BROWN: I wonder if the example
10 you quoted in the U.K. treasury treasury bill rate is
11 entirely pertinent, because over there so many other
12 things are tied to the bank rate.

13 MR. SHAW: To that I agree.

14 COMMISSIDNER BROWN: And that doesn't apply
15 here?

16 MR. SHAW: No.

17 COMMISSIONER BROWN: The other question I would
18 like to ask is if the bill rate is considerably below
19 the administered rate or the fixed bank rate, how
20 effective is this fixed bank rate?

21 MR. ELY: It becomes less effective if that
22 takes place and rather indicates that the fixed bank
23 rate should be reduced. The interest rates are tending
24 towards what the market-place thinks -- the way the
25 market place thinks the economy is going.

26 COMMISSIONER MACKINTOSH: Can I ask a question;
27 by a fair bid or by this open market operation, or both,
28 can the Bank of Canada fairly well control the bill rate?

29 MR. ELY: As you probably are aware, Dr.
30 Mackintosh, the Bank of Canada always -- there is always



1 a bid made by the Bank of Canada at each auction for
2 the entire issue in case there are not enough bids
3 from other money market concerns to take up the option,
4 so therefore they can have a very marked effect.

5 COMMISSIONER MACKINTOSH: What I am getting
6 at is if the bank rate is fixed and your bill rate is
7 5-1/8, or whatever it is, has the Bank of Canada the
8 tools to move the bill rate into what it thinks is
9 the proper relation?

10 MR. ELY: Yes, issue more bills.

11 COMMISSIONER MACKINTOSH: And maybe that is
12 the system?

13 MR. ELY: It is part of the system.

14 COMMISSIONER MACKINTOSH: And this problem
15 of the two being in conflict if the Bank of Canada
16 acts in this way ---

17 MR. ELY: If they take the proper action it
18 disappears.

19 COMMISSIONER MACKINTOSH: I don't think we
20 can devise any system that will work if the Bank of
21 Canada acts in a different capacity.

22 MR. ELY: Quite correct.

23 COMMISSIONER GIBSON: On the question of the
24 two kinds of rates; floating rates and tax rates, is
25 there much difference in the response in investment
26 dealers in their attitude and the advice that they give
27 their clients to the signals that are received to the
28 two types of rate. How do you respond to the floating
29 rate?

30 MR. COX: I don't think the floating gives



1 you much of a signal in the fact it moves a few points
2 from week to week. I don't think this is a basis for
3 advising your clients one way or another.

4 COMMISSIONER GIBSON: You don't regard it
5 as a signal generally?

6 MR. COX: No.

7 COMMISSIONER GIBSON: Even though the Bank of
8 Canada is a major factor in the market?

9 MR. COX: This is something you may or may not
10 know and they refrain from saying, or they may be buying
11 bills or selling bills for one of the government accounts.

12 COMMISSIONER GIBSON: This is your basic objection
13 to the floating rate, that it is ^{not} enough of a signal?

14 MR. COX: That is my objection, yes. I don't
15 know that I should speak for the association there.

16 MR. MILNER: In the past few years the floating
17 rate that we have was influenced by causes that had
18 nothing to do with the monetary supply outside of the
19 fact that if you had a very large delivery of , say,
20 Quebec Hydro and Ontario Hydro at the same time it
21 would affect the chartered banks in their loaning
22 position and you have a fluctuation of the bill rate
23 that wasn't caused by anything monetary, it was caused
24 by a delivery problem and the publicity in the paper
25 saying, "The bank rate goes up 11 points during the
26 week" and it didn't go up at all and there was no
27 change in the monetary policy.

28 COMMISSIONER GIBSON: This happens frequently.

29 MR. MILNER: Oh, it happens frequently.

30 MR. HUNTER: The bank rate is the only



1 indication other than the annual report which the
2 Governor publishes as to what his thinking is during
3 the year, and I think we all feel we would like to
4 know when he has changed his opinion about things
5 because the bank rate is virtually the only way we know
6 whether there is a strong market or not.

7 COMMISSIONER GIBSON: And this is something
8 which would happen only rarely?

9 MR. HUNTER: I shouldn't think it would happen
10 often.

11 COMMISSIONER GIBSON: How are you going to
12 run your money market if you just have a bank rate that
13 changes once in a long time?

14 MR. HUNTER: Well, I have been with a firm
15 and in the money market business and I don't like the
16 idea of the floating rate from this point of view,
17 but if were to run the risk of losing the fixed bank
18 rate I think we would invariably be prepared to work
19 on the bank rate rather than the bill rate.

20 THE CHAIRMAN: We shall adjourn now until
21 2.00 o'clock. We will not be through by 4.00 o'clock
22 this afternoon and I am saying this for the benefit
23 of those who have in mind leaving on the 4.00 o'clock
24 plane because I think it is pretty definite we will be
25 longer than that.

26 --- Luncheon Adjournment.
27
28
29
30



1 --- On resuming at 2.00 P.M.

2 THE CHAIRMAN: We will now resume.

3 COMMISSIONER BROWN: I wonder if I may ask a
4 question in connection with secondary reserve requirements
5 of the chartered banks. You recommend that the chartered
6 banks be released from the requirements on secondary
7 reserves. My understanding is that when this was
8 instituted one of the thoughts behind it was that by
9 forcing the banks if they wished to expand contra-
10 monetary policy to sell short-term Canadas which would
11 involve a greater loss that this would dissuade the
12 banks from taking this action, and we rather gather
13 from C.40 that you don't think this is quite operative.

14 MR. COX: I think the major objection I had
15 was this falls under the heading of moral suasion because
16 there is no legislation. The Bank of Canada persuaded
17 all the banks to agree to endeavour to maintain -- I
18 think that was the wording. This thing has been in
19 existence now for six years, and it is usurping the
20 power of government to legislate.

21 COMMISSIONER BROWN: Let me reword my question.
22 Do I gather from your remarks now that if this were made
23 part of the Bank Act that you would not have the same
24 objection?

25 MR. COX: I think this is something that probably
26 should be examined in greater detail, and that a fairly
27 good case can be made suggesting they are not particularly
28 effective if we are free to presume -- and I think we
29 should presume -- that the banks are going to follow
30 a normal, prudent policy of extending credit. Most of



1 the time since they have been in force the banks have
2 had essentially more than 15 per cent in cash and
3 secondaries. Therefore, it performs no useful function
4 other than perhaps getting some cheap money for the
5 government through treasury bill options by creating
6 a captive market.

7 On the other hand, when the banks find that
8 the loan demand is high, and these are good and proper
9 loans that they are making, they have to sell securities.
10 They won't sell bills; they will sell bonds. Presumably
11 this is a time when the Bank of Canada is trying to
12 tighten, and you may run the risk of a disorderly
13 market, if I may get back to that again, by the bank
14 having to reverse its monetary policy and acquire some
15 securities to prevent the market from dropping too
16 fast.

17 COMMISSIONER BROWN: I would like to have
18 your reaction to the suggestion that if the Bank of
19 Canada is trying to tighten things up, and if the
20 chartered banks have treasury bills which they can sell
21 without really costing them much, is this making it
22 more difficult for the Bank of Canada?

23 MR. COX: Do they not have to keep the treasury
24 bills to fulfill their secondary reserve requirements?

25 COMMISSIONER BROWN: If your suggestion were
26 followed out and they didn't have to keep the secondary
27 reserve ratio ...?

28 MR. COX: I see what you mean.

29 COMMISSIONER BROWN: I am asking for your
30 impression as to whether this would or would not make



1 it more difficult for the Bank of Canada to tighten
2 things up?

3 MR. COX: This would only be true to the
4 extent the chartered banks have excessive reserves --
5 they have more bills than they require or more day loans
6 than they require under the 7 per cent requirement.

7 COMMISSIONER BROWN: I think you misunderstand:
8 If they didn't have the 7 per cent requirement.

9 MR. COX: I see.

10 COMMISSIONER BROWN: Would that or would it
11 not make it more difficult for the Bank of Canada to
12 implement its monetary policy?

13 MR. COX: Well, I suppose it would if you
14 presume the banks won't be prudent and that they
15 are prepared to get themselves into an over-extended
16 position where they have no excess liquidity at all.
17 I don't think it would be a fair presumption that our
18 Canadian banks would put themselves in that position.

19 COMMISSIONER MACKINTOSH: Of course, if you
20 assume that (a) the banks are prudent and (b) prudence
21 requires 7 per cent treasury bills, then it doesn't matter
22 whether you have the regulation or not.

23 MR. COX: I don't know whether 7 per cent is
24 the right figure, sir.

25 COMMISSIONER MACKINTOSH: Whether it is
26 desirable or not, the whole practical effect is to
27 force the banks, if they are liquidating securities
28 in the face of Bank of Canada action to liquidate them
29 at some greater loss than if they took them, so to speak,
30 off the bottom of their treasury bill portfolio.



1 MR. COX: Yes.

2 COMMISSIONER BROWN: In effect, this makes
3 the central bank policy more quickly operative?

4 MR. COX: Under certain circumstances it would,
5 yes. I think our objection to the thing lay mainly in
6 the area that if it is deemed that this is a desirable
7 thing, when the time comes to revise the Bank Act in
8 1964, that this should be taken within the moral
9 suasion area -- the agreement area -- and legislated.

10 COMMISSIONER BROWN: This puts quite a different
11 aspect on your recommendation.

12 MR. COX: I think that is what I have said
13 in Section C, Mr. Brown.

14 COMMISSIONER BROWN: Your recommendation is
15 emphatically that the Commission consider recommending
16 that the agreement between the chartered banks and the
17 Bank of Canada in 1956 establishing secondary reserves
18 be terminated. Do I understand from your reply that
19 you really mean that it be terminated or established
20 by legislation? This is on page 7 of Volume I.

21 MR. COX: I am looking for the text in
22 Section C.

23 COMMISSIONER GIBSON: C.40 on page 22. You
24 say that it might lead to a disorderly bond market.

25 COMMISSIONER BROWN: I think there is no point
26 in pursuing it further because we have got your thoughts
27 on it, and it is not quite exactly what we understood.

28 MR. COX: I have got something here some place,
29 and I just can't find it.

30 COMMISSIONER BROWN: We might be able to come



1 back to it later. Then, in this context there is
2 another thing: If the secondary reserve ratio were
3 removed as a requirement what effect do you think
4 this might have on the availability of day-to-day
5 funds to the money market?

6 MR. COX: I think it would tend to increase
7 it.

8 COMMISSIONER BROWN: Would you like to develop
9 that a little bit.

10 MR. COX: Possibly someone in the money market
11 might be better qualified.

12 MR. HARRIS: This is a little difficult to
13 come to a decision on right away. I quite honestly,
14 not having thought of it, don't know the answer to it
15 immediately. At times I think it probably would
16 squeeze the money market when there was a pressure for
17 funds for cash position. At other times it might
18 go higher. The secondaries have been running around
19 19 per cent -- just recently they were well above the
20 the 15 per cent. One might presume the funds under
21 normal conditions would be available to the money
22 market that are now to the day-to-day loans, but I
23 would like to think about that one.

24 MR. MILNER: Do you want to comment further
25 on that, Mr. Cox?

26 MR. COX: No, I don't think I have anything
27 else.

28 MR. MILNER: Mr. Brown, would you want us
29 to give you a better answer on that later?

30 COMMISSIONER BROWN: I don't think we want to



1 recall you at all, but perhaps you might submit a
2 paper on it.

3 MR. MILNER: Would you like to say anything,
4 Mr. Ely?

5 MR. ELY: Yes, I think my view would be that
6 the 7 per cent moral suasion part of the 15 per cent
7 reserve should be enacted into the Bank Act, and that
8 if it was eliminated it would have a tendency in some
9 cases to have maybe too much money available, and in
10 other cases not enough; and I think it is working.
11 I think we have gone through some pretty troubled
12 times in the last few years and, by and large, I would
13 be of the view that it works. I would not think it
14 should be removed. I would think it should be put into
15 the Bank Act.

16 COMMISSIONER GIBSON: When you say it works,
17 what do you mean by that?

18 MR. ELY: If it were not there there might be
19 times when the chartered banks would channel some of
20 that 7 per cent into general loans. There might be
21 quite a few times when that would happen, and then there
22 would be less money available in that area to finance
23 the government's requirements in the bill market.

24 MR. HUNTER: May it not also have a tendency
25 to persuade the Governor to increase the cash reserve
26 requirements from time to time which would be an expensive
27 thing for the banks?

28 COMMISSIONER GIBSON: If you remove it?

29 MR. HUNTER: If you remove it: Not having
30 that additional 7 per cent protection you might then feel



1 it necessary to increase the cash reserve requirement
2 to 9, 10, 11 or 12 per cent ultimately.

3 COMMISSIONER LEMAN: Would you go so far as to
4 say there should be a variable reserve -- that the
5 Bank of Canada should be able to vary that 7 per cent
6 secondary?

7 MR. ELY: It is variable now, and I would think
8 when you inject it into the Bank Act there should be
9 leeway to vary it.

10 COMMISSIONER LEMAN: It should not be fixed
11 at 7 per cent?

12 MR. ELY: 7 per cent is a good figure, but
13 under certain conditions perhaps there should be some
14 leeway.

15 COMMISSIONER LEMAN: What makes 7 per cent
16 good?

17 MR. ELY: I suppose that 7 per cent figure
18 coupled with the 8 per cent cash figure came out of
19 experience and it has worked. That is what makes it
20 good.

21 COMMISSIONER BROWN: Would it work in another
22 period?

23 MR. ELY: Under certain sets of conditions
24 it would work -- under certain sets of conditions it
25 might be raised or lowered.

26 COMMISSIONER BROWN: Would this be in part
27 related to the availability of treasury bills?

28 MR. ELY: I don't think it should necessarily
29 be related to that.

30 COMMISSIONER BROWN: Would you see any danger



1 that if the government wished to finance more on a
2 treasury bill basis than they do so, and at the same
3 time increase the requirement to 10 per cent ...?

4 MR. ELY: I would hate to think that would be
5 the case, because that would be the wrong usage of it.

6 MR. SHAW: Isn't the test that it has worked,
7 or one of the evidences of it, the fact that the banks
8 as a rule are over a period -- and I am speaking strictly
9 from memory -- but isn't it the case that the banks
10 have maintained something more than the 7 per cent
11 rate much more often than they have crowded the 7 per cent
12 rate, and it has been more like 16, 17 or 18, and isn't
13 that the evidence that maybe this is a good level?

14 COMMISSIONER LEMAN: Don't you think if the
15 18 was the base they would try to be around 20 most
16 of the time?

17 MR. SHAW: If they are as conservative as we
18 know our banks to be ---

19 COMMISSIONER BROWN: To give themselves a
20 cushion?

21 COMMISSIONER LEMAN: They don't want to be
22 locked in the situation more than anybody else, so if
23 you make it 19, they will hover around 20 or 21.

24 MR. SHAW: Perhaps my assumption is wrong.
25 It seemed to me, observing over the years, that they
26 seemed to be more often comfortably above than just
27 crowing it within .1 or something.

28 COMMISSIONER LEMAN: That is the same -- to
29 have a little cushion or a little leeway. What proof
30 is there that 7 per cent is good? Mr. Ely says it



1 has worked. Perhaps what is meant is that a secondary
2 reserve works. We are talking about 7 per cent. Is
3 there any magic in 7 per cent?

4 THE CHAIRMAN: I would like to know what you
5 mean by saying it works. What do you mean by that?
6 There is the 7 per cent reserve which has been adhered
7 to: What do you mean by saying it works?

8 MR. ELY: What I meant by that, Mr. Porter,
9 was that that 7 per cent relates to the amount of
10 money available in the chartered banks for the purchase
11 of treasury bills, and the amount of money that the
12 government wanted to raise in that area -- the banks
13 throughout the 7 per cent reserve seem to have been able
14 to absorb it fairly easily and comfortably. So, it
15 works in the context that the number of bills that are
16 issued at the weekly auction and the 7 per cent seem
17 to go together comfortably.

18 COMMISSIONER GIBSON: Mr. Milner, you have
19 some disagreement in your association in this matter.
20 Mr. Cox suggests it does not work and it creates a
21 disorderly condition in the market at times; isn't that
22 right?

23 MR. COX: It might.

24 MR. MILNER: Well, Mr. Gibson, if you will follow
25 our brief as a whole we have endeavoured not to dictate
26 or to suggest specific things which we believe to be
27 out of our province. For instance, when we come to
28 the matter of what we call the near banks we do not
29 suggest that a regulation covering near banks should
30 be modeled after the reserves of the primary. We don't



1 know that is the correct basis or not. We merely
2 say we think the government should have some control
3 over the loaning policies of the near banks, but as
4 to what that control is we don't feel ourselves capable
5 of giving a reasonable opinion, and when we come to
6 the subject of the secondary reserves of the chartered
7 banks we merely point -- and I don't think there is
8 quite the disagreement which you are inferring -- we
9 point out that in the last three or four years this
10 moral suasion with the 7 per cent reserve has never
11 come close to the 7 per cent. The banks have crowded --
12 and quite rightly so -- the 8 per cent cash reserve
13 because that is where they make their extra remuneration.
14 In other words, if a chartered bank were to run to
15 9 per cent primary reserve it would not make as much
16 money as a bank that ran on an 8 per cent reserve.
17 But when it comes to moral suasion, we feel that moral
18 suasion over a long period of time is not the correct
19 approach to either proper banking or proper finance.

20 THE CHAIRMAN: That is one aspect of it: Whether
21 or not it should be statutory. But still I would like to
22 know a little more about why it is necessary to have
23 any provision at all for that 7 per cent. There are
24 the two views that are expressed, and there may not
25 be much more to be said about it.

26 MR. BEATTY: In competition in business,
27 Mr. Chairman, it is very frequently helpful to have
28 some rule-of-thumb which enables you to tell your
29 customer, "Much as I like you, beyond this point I
30 cannot go."



1 COMMISSIONER BROWN: What is the context?

2 THE CHAIRMAN: I don't know that I am any
3 wiser.

4 MR. BEATTY: If you have a 7 per cent require-
5 ment which you cannot go beyond, then it is easier to
6 explain to your customer that you cannot serve his
7 need at this time.

8 COMMISSIONER LEMAN: I think one should keep
9 the very important fact in mind here that, moral suasion
10 or not, the fact is that the bank has the right to
11 vary the primary reserve. If the bank found the banks
12 not keeping the right amount of secondary reserves,
13 they always have the threat of moving the primary
14 reserve, don't they?

15 MR. MILNER: That is correct, Mr. Leman. As
16 I understand it, so far there has been no change ever
17 in the primary reserve since it was inaugurated --
18 since a definite percentage was put on, and we merely
19 suggested that rather than having a moral suasion
20 clause for the secondary, that surely the government
21 could better operate the system by varying the primary
22 reserve to some extent if necessary.



We just do not believe that moral suasion is the proper method of operating over a period of years. It could happen over a short period under stringent conditions such as existed a few years ago when the government did not want any more finance paper issued. At one time they did not want any non-essential buildings constructed, they used the moral suasion clause to ask the chartered banks not to lend money to non-necessary activities, but that did not remain in force over any particular period. This particular moral suasion has been in for --

MR. COX: Just about six years.

MR. MILNER: For six years we have had the same clause in the moral suasion.

COMMISSIONER BROWN: We have some things to say about moral suasion as such later on and I think we would rather deal with them in that context.

MR. MILNER: All right.

COMMISSIONER BROWN: In this case I am speaking about secondary reserves.

MR. COX: Mr. Brown, I have found what I was looking for, C.88 and it comes under a matter requiring further examination and discussion.

It says:

"The Commission might examine whether chartered bank secondary reserves which were instituted through moral suasion in 1956, should continue to remain in effect."

I do not think that is a recommendation.

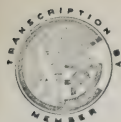


1 COMMISSIONER BROWN: Well, what is this
2 recommendation 26? I wonder if we might move along.
3 In B.25 reference is made to the way in which the
4 liquidity on ease of market ability of long term
5 Canadas has declined and the implication is there
6 that the previously prevailing yield spread between
7 provincials and municipals relative to Canadas has
8 narrowed. Would you care to comment on that?

9 MR. MILNER: Well, Mr. Brown, I think
10 most of that was covered in the discussion before
11 lunch where we were referring to the market for
12 Canada bonds. Perhaps Mr. Ely would like to expound
13 a bit further on it.

14 MR. ELY: As you wish. I think I pointed
15 out the development that had taken place and that
16 there was an attitude on the part of the investor
17 both institutional and private to buy securities
18 of provinces which gave a somewhat greater yield
19 and through experience they had found it just as
20 good as marketability goes if not better in some
21 cases, and that the federal government had used up
22 their retail market through the issue of savings
23 loan bonds. The reason for that paragraph, I suppose,
24 was that in the case of provincial securities there
25 has been a more continuous and better market than
26 there has been for long term federals probably due
27 to the fact that there are sinking funds in every
28 province and no sinking fund exists in the federal
29 area.

30 COMMISSIONER BROWN: This brings up the



1 recommendation which comes up elsewhere about the
2 question of sinking funds for federal bonds.

3 MR. ELY: That is right.

4 COMMISSIONER BROWN: Do you think this is
5 a very material factor in the marketability and the
6 liquidity of long term Canadas?

7 MR. ELY: Yes.

8 COMMISSIONER BROWN: Has this always had
9 an effect on the liquidity of bonds? I would like
10 to have your comments, for instance, on Bell Telephones.

11 MR. ELY: A little louder, Mr. Brown.

12 COMMISSIONER BROWN: I was wondering to
13 what extent this sinking fund always has an effect
14 on the marketability you mention. I am thinking of
15 Bell Telephones where there is no sinking fund.

16 MR. MILNER: Mr. Brown, we believe that
17 the Bell Telephone would have a better secondary
18 market had they had a sinking fund but literally the
19 institutions as a whole, that is, the insurance companies,
20 trust companies, et cetera, prefer to purchase -- naturally
21 they have an increase in return by so doing -- to purchase
22 all corporation bonds with a sinking fund. A
23 corporation sinking fund is the highest of all sinking
24 funds excluding Bell Telephone but there is a con-
25 tinuous market through the sinking fund operation
26 for corporate bonds and in the case of the provinces,
27 the western provinces particularly, -- take Saskatchewan
28 as an example. Saskatchewan had originally one of
29 the worst credit ratings in Canada. When they re-
30 organized their whole debt structure and put their



1 sinking fund down, the 3 per cent sinking fund has
2 created a market for Saskatchewan bonds that, in our
3 view, has been a wonderful attribute to the province
4 and to the market as a whole.

5 Any sinking fund, if properly administered,
6 acts as a secondary market if you want to call it such
7 from the 1st of January to the 31st of December because
8 sinking funds do not normally purchase all their
9 requirements the first day and have no market afterwards.
10 The properly administered sinking fund purchases their
11 securities with the viewpoint of maintaining their
12 credit rating as high as is possible.

13 MR. SHAW: I wonder if you would want to
14 restate the early part of your remark, Mr. Milner?
15 I do not think you intended to say that Saskatchewan
16 has one of the worst credit ratings.

17 MR. MILNER: No, I said originally it
18 had one of the worst.

19 MR. SHAW: It came through to me without
20 the word "original".

21 MR. ELY: I think we can resolve the
22 question, as this is my part of the brief, by saying
23 that the attitude of the investor is such that he
24 is quite prepared to buy provincial, municipal
25 and corporate securities where in many cases there
26 is just as good a market and where the yield is greater.

27 COMMISSIONER BROWN: Would I be correct
28 in restating your point that the yield spread between
29 provincials and Canadas is now on such a constant
30



1 basis that if there is marketability within that yield
2 spread that you might as well have the benefit of the
3 greater yield?

4 MR. ELY: That is right. Sometimes the
5 market for Dominion of Canada bonds has been put to
6 a level one way or the other that perhaps does not
7 sometimes suit the investor but there is no such
8 things that work with provincial bonds. They work
9 in a completely free private market.

10 COMMISSIONER MacKEEN: Do you see, Mr. Ely,
11 a situation where it might react against the borrower
12 having a sinking fund? I am referring to the case
13 of private placement where there are perhaps half
14 a dozen or a dozen institutions owning bonds and then
15 no matter what the interest rate might be the bonds
16 are not available below the call price for sinking
17 fund purposes.

18 MR. ELY: That has been the case, Mr.
19 MacKeen.

20 COMMISSIONER MacKEEN: It is rather a grievous
21 situation from the borrower's point of view.

22 MR. ELY: It does not happen too often but
23 it is an onerous situation on the borrower if market
24 conditions have carried the price down and they cannot
25 buy them. I think they should give some consideration
26 also to the man who lends them the money at that low
27 rate and they can always call them.

28 COMMISSIONER MacKEEN: They can call a 4 per
29 cent at 1.05, for instance.
30



1 MR. ELY: That is right.

2 COMMISSIONER MacKEEN: Twenty years.

3 MR. ELY: Yes.

4 MR. MILNER: That was the penalty, Mr.
5 MacKeen, of the borrower at the time of the issue
6 deciding that he would sooner pay 4 per cent rate
7 privately than he would a $4\frac{1}{4}$ per cent rate publicly.
8 The cost of a private placement -- this, of course,
9 is more true particularly in the American market
10 where there is a huge amount of private placement
11 and you have situations there where they are calling
12 a 3 per cent bond at 1.03 merely because they are
13 only owned by one person.

14 COMMISSIONER BROWN: I think if we can
15 get back to the discussion of the operation of the
16 Canada market. In C.21 there is a reference to the
17 fact that the Bank of Canada has consistently under-
18 estimated the psychological effect of its market
19 operations which periodically has created excessive
20 speculation and something resembling panic. We
21 touched on this this morning but I wonder if we could
22 have a little further discussion on just what is
23 meant by this. Is this a matter of operation by
24 the Bank of Canada, the way they operate?

25 MR. COX: I think it perhaps stems from
26 that from time to time, but I have a feeling that
27 while they must realize it they tend to disregard
28 the fact that the Bank of Canada is not an investor
29 in the sense that insurance companies, banks, et cetera,
30



1 are investors. They are not looking for a return of
2 their money; they only own securities as a result
3 of having changed monetary policy or to enable them
4 to change monetary policy and as the biggest factor
5 in the market when they start doing something every-
6 body tries to figure out what they are trying to do.
7 Perhaps undue stress is placed upon what might be a
8 very innocuous little operation on one of the government
9 accounts and it becomes interpreted as a major change
10 in monetary policy.

11 COMMISSIONER BROWN: Would you like to go
12 on and discuss the problems that occur, if there
13 are such problems, in the operation of Canadian desks,
14 both in Montreal and Toronto?

15 MR. COX: I think we tend to feel that the
16 trading departments in both Montreal and Toronto are
17 not large enough and I think usually a dealer cannot
18 reach the trader because there is usually only one
19 in the city and has to wait for a call back. He
20 wants to do something right away. The fellow under-
21 takes to call him back. He is not given enough
22 discretion and it seems to periodically create a
23 situation where a trader gets an additional sale if
24 he does not call you up in an hour he is not going to
25 do it. He is probably off his bid or off his offer
26 and this seems to spread into the whole trading
27 community and everybody starts testing the bank to
28 see if they are there or not and you have got this
29 situation where a dealer may have one million and
30 sell you a quarter and give you a quarter of a million,



1 and a quarter of a million from somebody else and he
2 is paying a higher price to another dealer. This
3 seems to be unnecessarily complicated. Perhaps
4 somebody else would like to comment on this matter.

5 MR. MILNER: I think Mr. Hunter would
6 like to comment on this.

7 MR. HUNTER: Well, it gets back to what
8 was mentioned this morning, that the Bank of Canada
9 during the past few years has been the focal point
10 in the market for government of Canada securities.
11 Nobody wants to make a move until he finds out what
12 the bank does. The trader goes in and makes an offer
13 at the level at which he thinks the bank is and the
14 trader there says: "I will have to let you know"
15 and it might be necessary for him sometimes -- some-
16 times it is reasonably fast, it might be 15 or 20
17 minutes or it may be as long as two to three hours.
18 Now, what do you do in the meantime? Do you just
19 sit and wait? By this time everybody gets a little
20 tense and wonders what should be done. This is
21 the sort of situation that is created in the street
22 and by the time the first dealer is able to sell
23 a few bonds there are half a dozen other dealers in
24 selling because they feel there is this development
25 occurring and all this accelerates along the line.

26 COMMISSIONER BROWN: How do you suggest
27 this should be improved?

28 MR. HUNTER: We suggested this morning
29 that the Bank of Canada should not operate in the long
30



1
2 term market and possibly that is the most definite
3 answer.

4 COMMISSIONER BROWN: I gathered there
5 was a difference of opinion that some people felt
6 that they should. Among those that felt that the
7 Bank of Canada should operate how could this be
8 improved?

9 MR. ELY: I thought they should operate
10 in the long term market. I completely agree with
11 Mr. Cox and Mr. Hunter that it could be improved
12 and improvement would come about through more Bank
13 of Canada traders in both markets and more authority
14 so that they could act properly and there would
15 not be this confusion and there would not be a time
16 lag that creates what Mr. Hunter said.

17 MR. WADDS: Mr. Brown, the solution that
18 comes to mind that may or may not be practical is
19 if they removed the trading operations completely from
20 Montreal and Toronto and put them in Ottawa and had
21 a bunch of open lines into Montreal and Toronto. The
22 authority for their operations all comes from Ottawa
23 anyway and from a mechanical standpoint our trading
24 departments could pick up a telephone and get the
25 trader in Ottawa where the authority is. I thought
26 that would eliminate a lot of this delay.

27 MR. HUNTER: I do not know if we are
28 competent to advise the Bank of Canada how they
29 should direct their trading operations because it
30 may not refer to their actual operations at all; it



1 may be a matter that they are dealing with their
2 problems in regard to the monetary picture. They may
3 be making a decision as to whether they want to move
4 it up or not.

5 COMMISSIONER BROWN: There is nothing about
6 the mechanics of it.

7 MR. HUNTER: But I am suggesting the mechanics
8 themselves might not be completely at fault. It might
9 be those at the bank who could not make decisions for
10 certain reasons.

11 COMMISSIONER BROWN: There appear to be two
12 areas in which in your opinion there should be improve-
13 ment. One is decisions and the other is the mechanical
14 operation of getting in touch with people and getting
15 word back again. We have heard a suggestion that instead
16 of performing both monetary --

17 MR. HUNTER: It is purely a personal opinion.

18 MR. MILNER: Mr. Brown, if I might just
19 put this. The opinion of most of our members, that is,
20 who are really actively trading in government issues
21 is that the Bank of Canada security department as such
22 is definitely understaffed. It must be understaffed
23 on account of the time lag that occurs. The in
24 between -- normally a dealer in securities, if you
25 want to call it the street dealer -- you can get
26 immediate answer on the telephone as to whether you
27 are willing to buy or sell a security and the frustration
28 occurs, the delay occurs when the Bank of Canada, as
29 Mr. Cox and Mr. Hunter have said, will say: "We will
30 have to telephone you back."



1 As Mr. Cox said, it could be a bank policy, but we
2 are under the impression that there is not sufficient
3 authority given to the people who are contacting dealers
4 on the telephone. Before stating that as a fact I
5 would like Mr. Harris to express his views.

6 MR. HARRIS: I am thinking of the money market
7 again.

8 These delays are often more important when
9 you get down to shorter bonds, and the same thing occurs
10 there. I think the money market dealers have largely
11 eliminated the problem between Toronto and Montreal.
12 The dealers have direct lines between the two cities.
13 We move large amounts very quickly, but under many
14 circumstances the bank system often moves on short-term
15 securities. The Bank of Canada has a very important
16 role in the money market. Certainly it does not intend
17 to operate in the short-term money market in most
18 cases.

19 These delays of some periods are often serious.
20 The problem is that one trader usually in Montreal and
21 Toronto deals with the money market and long-term
22 securities both. If the trader is absolutely fully
23 engaged all the time he has no chance to sound the
24 market out at all. I think this is a problem also.
25 The trader does not have the time to talk to the banks
26 and dealers in a general way so as to know what is going
27 on, and know what the other factors are in the market,
28 and to know what sort of rumours are in the air in
29 regard to possible other financing which may affect
30 the rates on this type of thing. I think quite honestly



1 within both centres of Toronto and Montreal they know
2 what factors are taking place in the markets more
3 than they did. I think the dealers are in contact with
4 Ottawa. They have often informed us of conversations.
5 They are not right in contact. This is again a problem
6 in the money market. There is certainly not enough
7 attention paid to the particular money market policy
8 and the speed required in these centres.

9 COMMISSIONER BROWN: Is there any criticism
10 implied or otherwise regarding the skill of the persons
11 employed?

12 MR. MILNER: No. I think, Mr. Brown, the
13 criticism, if you might term it such, and I think if
14 you were to question the chartered banks you would find
15 the same reaction there--because they desire to act
16 quickly^{and}/because of necessity they must at certain times--
17 that the inefficiency, if you want to term it as such,
18 is a result of their being under-staffed. There is
19 literally, in our opinion, not a large enough staff.
20 We think that the Bank of Canada marketing operations
21 are under-staffed.

22 COMMISSIONER BROWN: In regard to the question
23 of debt policy, you suggest that the national debt
24 should be held by as great a number of individuals,
25 institutions and corporations as possible. I think
26 that statement appears in Section B, paragraph 22.
27 What are the advantages of this wide distribution in
28 the field of debt management, and the effect on monetary
29 policy?

30 MR. SHAW: Is this question directed to me?



1 MR. MILNER: Yes, would you answer that.

2 MR. SHAW: The first question is, what are the
3 advantages of the wide distribution of holders of
4 government debt?

5 COMMISSIONER BROWN: Yes. The American federal
6 debt does not seem to be as widely distributed in terms
7 of individuals so far, as compared to Canada.

8 MR. ELY: This is a section that I wrote,
9 Mr. Brown. I think perhaps I should answer the question.

10 MR. SHAW: Yes.

11 COMMISSIONER BROWN: I am not going to allocate
12 the question, that is up to Mr. Milner.

13 MR. ELY: The question is directed toward a
14 portion of the brief for which I am responsible. I
15 said the national debt should be held by as great a
16 number of individuals, institutions and corporations
17 as possible. The reason for saying that is this.
18 The greater number of people that own federal securities;
19 one, the greater interest they will take in the country;
20 and two, the broader and deeper the market will be for
21 the instrument that the government used to raise this
22 money. In my opinion those are both sound reasons why
23 this should happen to the greatest extent possible.

24 COMMISSIONER BROWN: We seem to have had
25 indications also, and I think this appears elsewhere
26 in the brief, that individuals particularly buy federal
27 securities with the idea of security of principal.

28 MR. ELY: That is right.

29 COMMISSIONER BROWN: And of marketability?

30 MR. ELY: That is right. This is something that



1 we should strive to attain. It is not something that
2 is presently in existence.

3 COMMISSIONER BROWN: The thing I am trying
4 to get at is your thinking that if monetary policy is
5 going to have an effect these bonds are going to change
6 in price.

7 MR. ELY: That is right.

8 COMMISSIONER BROWN: And therefore the individual
9 must get educated, must he?

10 MR. ELY: Yes.

11 COMMISSIONER BROWN: To the fact that his
12 bonds are going to change in price?

13 MR. ELY: Yes, but if he is an investor that
14 does not make much difference to the Dominion of
15 Canada bonds.

16 THE CHAIRMAN: It makes a difference if he
17 has to sell the bond all of a sudden for some reason?

18 MR. ELY: Yes, he has the opportunity.

19 THE CHAIRMAN: If the price of the bond is
20 down on the market he may not be encouraged to buy
21 another bond in the future.

22 MR. ELY: He may also be not encouraged to
23 sell at a time when it is probably wise to have that
24 money invested rather than spent when the economy is
25 under pressure.

26 MR. SHAW: I think I see the Chairman's point
27 of view. Harkening back to our Victory Loan bonds
28 and subsequently, under the most intense kind of
29 publicity or propaganda promotion, if you like, we induced
30 the public to invest its savings in the highest quality



1 of security available, and we put forward the suggestion
2 that if you do this you defer these needs of yours
3 until some time later, and always you are going to be
4 able to convert it into cash. We also use the argument
5 here that if you have a sudden need for money it is
6 almost as if you had money in the bank. I think your
7 suggestion was that there are dangers involved.
8 First a kind of danger arises when a great many
9 individuals having been induced to entrust their
10 savings into this particular instrument or type of
11 investment, and the value of these investments declines
12 and the purchasing power of the income derived from
13 them declines; that in itself may create problems. Unless,
14 Mr. Brown, you were thinking also of the lack of
15 effectiveness in monetary policy if your debt is spread
16 out over a great many individuals in a wide area where
17 you cannot get at it, reducing the buying and selling of
18 government bonds. That danger I would think is
19 minimal because we now have a large enough body of
20 short-term investment in the banking system to permit
21 us not to have monetary policy diluted by wide ownership.

22 COMMISSIONER BROWN: I was wondering if you
23 would also care to comment on the extent to which
24 Canada savings bonds are impinging on what would be the
25 normal market, or the otherwise market, I should say,
26 for fixed income federal bonds.

27 MR. MILNER: I would like to answer that
28 question, Mr. Brown.

29 When the war was over the government and
30 the Bank of Canada at that time were intensely interested



1 in maintaining these savings that they had induced
2 through the purchase of Victory loans. They tried to
3 find an instrument that would be compatible with
4 keeping public interest in our securities. Before
5 going any further, as far as I am concerned, I think
6 that to compare our position with the United States is
7 erroneous to start with. The American nation is a
8 supplier of world capital. We are a borrower of capital,
9 or have been over the past generation as a growing
10 country. So that the American debt structure I do
11 not think can be compared with ours. I think that
12 our debt structure, with our huge amount of debt
13 distributed in the hands of the public, is a far
14 safer factor for a borrowing country than the American
15 system of having it concentrated in a limited number
16 of sources.

17 To go back to the Canada Savings question,
18 they were brought out shortly after -- I forget when
19 the first issue was, but shortly after the war. They
20 were brought out to encourage the continuance of
21 savings among, if you want to call it, the working class
22 people; the labour population of the country. I refer
23 to the big labour force involved in the large industrial
24 plants, and through the efforts largely of members of
25 our association who covered all those plants, they
26 were able to persuade the industrial companies to
27 assist in the canvassing of their employees on a
28 continuous basis, having an annual Canada Savings loan
29 on which the money was absolute. Any time the money
30 was needed it could be turned in at 100 cents on the



1 dollar. Added to that they wanted to encourage the
2 normal thrift of citizens at large who were not working
3 in the big industrial plants.

4 They started off at a limit of \$2,000 in
5 savings loans. We as an industry are thoroughly in
6 accord with the principle of Canada Savings bonds. Where
7 we disagree with the government is that we think the
8 government in the last few years has tended to make it
9 a borrowing situation rather than a savings situation.
10 When they raised the amount to \$20,000 per person it
11 was obviously no longer a savings situation. People
12 do not save \$20,000.

13 COMMISSIONER BROWN: Not even among the
14 investment dealers?

15 MR. MILNER: Except some of the wealthier
16 ones.

17 It became a means of raising money. We do not
18 think that the government should raise money through
19 call money at a high rate of interest such as has been
20 obtainable in Canada Savings loans, because these
21 loans originated for the purpose of supplying savings
22 instruments.

23 We were talking either yesterday or this
24 morning about the fact that this has been copied to
25 some extent by our provinces who decided this was a
26 lovely way of raising money. It has now gone to our
27 municipalities. We have got treasury bills in nearly
28 all of our large cities, and it has even got down to
29 practically the villages which are willing to borrow
30 money on short-term bases. That was call money on



1 short-term bases.

2 All we have said in our brief in respect to
3 Canada Savings bonds is that we do not believe it should
4 ever be used as a money raising device, but should be
5 confined to a savings device.

6 THE CHAIRMAN: May it partly be due to the
7 fact that people were reluctant to buy bonds when
8 they found that they might have to sell at a loss,
9 whereas in respect to savings bonds they are sure of
10 getting their capital back? Is that not one of the
11 advantages?

12 MR. MILNER: I think, Your Honour, to some
13 extent that is probably true, but I think we have
14 developed an image over the past 10 or 15 years, and
15 the nation as a whole is investing a large portion of
16 its savings annually in Canada Savings bonds. I am
17 speaking of purely savings. Whether it be against
18 purchasing a house two years from now or not makes no
19 difference.

20 THE CHAIRMAN: I say, this is an attraction?

21 MR. MILNER: There is an attraction.

22 THE CHAIRMAN: Particularly in respect to
23 individual investments.

24 MR. SHAW: It is a defence against the
25 experience in some of the market issues.

26 THE CHAIRMAN: Yes.

27 COMMISSIONER BROWN: My question was, to what
28 extent do you think this inhibited the Government of
29 Canada borrowing on a long-term basis.

30 MR. MILNER: I think I am speaking for our



1 whole industry when I say that we believe that if
2 the limit of the available purchase is confined to
3 a reasonable amount that it does not affect the
4 ability to borrow long-term but, mind you, it must take
5 off, of necessity, some of the short-term money.

6 By and large the people who purchase Canada Savings
7 bonds are not the same people who purchase long-term
8 securities, to a marked degree. They are when you get
9 up to \$10,000 or \$20,000.

10 COMMISSIONER BROWN: My question, to what
11 extent do you think that the issue of Canada Savings
12 bonds in recent years has inhibited the federal government
13 from borrowing on a long-term basis? Has it had any,
14 and if so, to what extent?

15 MR. MILNER: To a considerable degree. My
16 own personal view is that \$5,000 is the absolute limit
17 that should be permitted in Canada Savings bonds.

18 COMMISSIONER BROWN: Then is it your suggestion
19 that all sales to individuals of above \$5,000 might
20 have been put into longer-term bonds?

21 MR. MILNER: No, I do not think so, Mr.
22 Brown. I do not know what the proportion is, but even
23 call it 50 per cent; that might have gone into long-term
24 bonds. It certainly is not 100 per cent, or not even
25 close to that. If you look at the results of Canada
26 Savings bonds sales you will see that payroll savings
27 represents the biggest amount in these bonds.

28 COMMISSIONER BROWN: What I am trying to get
29 at is, you criticize this way of raising money for
30 the government. My question is, if it did not raise



1 this money, what proportion of it might have been
2 raised through straight term debt securities?

3 MR. MILNER: I would say 15 per cent, possibly.

4 COMMISSIONER BROWN: Then it has not been a
5 big factor?

6 MR. MILNER: In preventing long-term, no.

7 COMMISSIONER BROWN: So it has raised money
8 for the government that would not otherwise have been
9 raised?

10 MR. MILNER: I think they used this as a money-
11 raising device, and at this high limit it definitely
12 took it away from the savings aspect. It was no longer
13 a savings bond, it was an investment. The establishment
14 of the \$20,000 limit has affected the ability of the
15 Province of Quebec to distribute securities. Why would
16 anyone purchase a Province of Quebec security if he
17 could buy a Canada Savings bond guaranteeing 100 cents
18 on the dollar at any time of the day or night?

19 MR. ELY: May I speak in this regard?

20 I think the Canada Savings loan issues have
21 to a very marked degree usurped the market of other
22 worthy borrowers, and have taught them to buy something
23 which is very favourable in their hands, but it has
24 certainly taken the market away from other people who
25 wish to borrow. Is that what you are trying to ask?

26 COMMISSIONER BROWN: Yes, but I am also asking,
27 how would the federal government have raised the same
28 amount of money on a straight term loan? Apparently
29 not through the same feature.

30 MR. BEATTY: To some extent through the same way.



1 COMMISSIONER BROWN: The answer was 15 per
2 cent.

3 MR. ELY: My view would be that in the days
4 of the original inception it would be a great deal more
5 than 15 per cent. As the public has been educated to
6 buy Canada Savings bonds over a period of 14 years
7 the percentage has gone down, but had this instrument
8 not been used to the extent it has been, as a major
9 money raising vehicle, the other market that they took
10 over by issuing savings bonds would have been large
11 enough to have financed the government's normal
12 requirements.

13 COMMISSIONER BROWN: The next question is, in
14 the current market what sort of a rate do you think
15 should be put on Canada Savings bonds in respect to
16 this payroll savings feature that you discussed earlier?

17 MR. ELY: In the current market?

18 MR. MILNER: You mean today's market?

19 COMMISSIONER BROWN: Yes. What I am trying
20 to get at is, to what extent do you think the interest
21 rate is a factor in payroll savings plans?

22 MR. SHAW: It has to be sufficiently above the
23 rate that would be obtained on savings deposits to
24 attract into this vehicle, as against leaving it in
25 the bank. It should not go beyond what a test would
26 show to be a sufficient incentive to persuade the
27 individual -- the man on a payroll savings plan or
28 what have you -- to accumulate savings in this way.

29 COMMISSIONER BROWN: I am asking you to guess
30 at the appropriate level.



1 MR. SHAW: The appropriate level, if they
2 were doing it now?

3 COMMISSIONER BROWN: I refer to the payroll
4 level.

5 MR. ELY: Oh, I would say 5 per cent.

6 MR. HUNTER: I think that is too high. I
7 think that has been one of the problems in regard to
8 Canada Savings bonds. Not only have they increased
9 in size, they have made the rate comparable to the rate
10 of a public issue. This is a wonderful instrument for
11 anyone to buy. Any individual who can find \$10,000
12 a year to invest would find no incentive to invest any
13 place else because he gets virtually the same rate
14 from Canada Savings bonds as he would on the open market.
15 I think if the individual is getting the privilege of
16 getting his securities in savings bonds he should expect
17 a lesser rate. From an imperial savings point of view,
18 my feeling would be that a 4 per cent rate is all that
19 should be offered for these bonds.

20 MR. SHAW: Now, or when the 5 per cent rate
21 was first introduced? In relation to the price on
22 the market perhaps it is more realistic.

23 MR. HUNTER: I think they have got it out of
24 line. I think they went too far with the rate.

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Nethercut & Young

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FOLLOWS

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1 MR. ELY: By and large the rate that they
2 have issued Canada savings loan bonds on has usually
3 been -- I think you will agree -- at one-quarter
4 of one per cent less than that.

5 MR. HUNTER: I would say that is about
6 right.

7 MR. ELY: On other term Canada issues?

8 MR. HUNTER: That is right.

9 MR. ELY: Now, today when I was trying
10 to measure the five per cent as of now, I am measuring
11 it against the value of long term Canada as of now,
12 and that rate is probably 5.65 or 5.70.

13 COMMISSIONER BROWN: I think what I am
14 trying to get at is that there are two elements in
15 the Canada savings bonds and I believe I understood
16 from Mr. Milner's remarks that he is in favour of
17 this on the payroll end of it.

18 MR. MILNER: That is right.

19 COMMISSIONER BROWN: That type of saving,
20 but not so much in favour of being in competition
21 with what could be normal/^{market}securities. My question is,
22 could you estimate an opinion as to how important
23 the interest rate structure is in this payroll part
24 of the operation?

25 MR. HUNTER: I do not think it is very
26 important at all.

27 MR. ELY: Not as important if they are
28 only going that far, and that is why I suggested
29 perhaps today you could get three-quarters of a point
30 away from the existing yields of other Canadas, whereas



1 they use a level of about one-quarter of a percent
2 away. You might even go further.

3 COMMISSIONER BROWN: One further question
4 on this. Do you consider that the general level
5 of the Canadian savings bonds interest rates has
6 been too high?

7 MR. ELY: They could not have raised
8 the amount of money they have raised had they had
9 it at a lower level.

10 COMMISSIONER BROWN: Thank you. Now,
11 you make a recommendation and this is 21 and 22.

12 MR. SHAW: What section?

13 COMMISSIONER BROWN: I am sorry, I beg
14 your pardon. That is not the one, it is recommendation
15 10:

16 "...that a standing committee composed
17 of men from The Investment Dealers'
18 Association of Canada having experience
19 and independent judgment in the marketing
20 of Government of Canada bonds be
21 established by Government decree
22 to act in an advisory capacity to
23 the Bank Of Canada and the Department
24 of Finance in connection with such
25 matters as the marketing of Government
26 of Canada issues and open market and
27 trading operations."

28 MR. MILNER: I will ask Mr. Cox to speak
29 to that.
30



1 MR. COX: We think that both the Department
2 and the Bank could benefit from additional information.
3 I do not think that any of us have the idea that this
4 committee would be absolutely perfect to the nth
5 degree in the advice they are able to provide either
6 to the Bank or the Department, but frequently two
7 heads are better than one, and to the extent it
8 was composed of, say, dealers -- we are the people
9 who are contacting the accounts and will be doing
10 the business -- and bankers who are people who have
11 some idea what the situation is and I think that
12 firsthand knowledge is better than something a bank may
13 or may not have picked up, and considerable use
14 of this sort of committee is made by both the Federal
15 reserve and the treasury department in the States
16 and we think perhaps it is worth a try.

17 Do you have anything further on that?

18 MR. ELY: I am in complete agreement
19 with you, Mr. Cox and I would like to say something
20 else on this, that in effect this is going on now,
21 but it is going on on a hit or miss basis by various
22 telephone calls that may or may not be initiated in
23 Ottawa or in Montreal and we think that it should be
24 focused properly and the government could get better
25 advise.

26 COMMISSIONER BROWN: Who would choose the
27 personnel?

28 MR. ELY: I think the only people that
29 can choose it, really, are the finance department
30 in consultation with the Bank of Canada because they



1 know -- those two areas know the people with the
2 best knowledge, and it should not be chosen on a
3 regional basis or anything like that, it should
4 be chosen purely on a matter of knowledge and
5 ability, and they have the ability to choose these
6 men.

7 COMMISSIONER BROWN: Do you think they
8 should meet regularly?

9 MR. ELY: I would think that they should
10 meet at regular intervals and at several times when
11 they have in mind doing some financing. This is
12 the sort of thing that goes on in United States;
13 they have a standing committee and they go to
14 Washington and it has worked very well, I understand.

15 THE CHAIRMAN: It would be somewhat
16 similar to the relationship between the provincial
17 government and the syndicate?

18 MR. ELY: That is right.

19 THE CHAIRMAN: It would be the same type.

20 MR. ELY: We have never brought provincial
21 issues to the market; the industry have never brought
22 the provincial issue to the market to my knowledge
23 without having prior consultation with what we like
24 to call a steering committee, and that steering committee
25 is made up of the knowledgeable people in the syndicate
26 involved. The same technique could be applied
27 in the federal area because it has worked and you
28 can see the results of it in the marketplace.

29 COMMISSIONER GIBSON: And what would you
30 talk about? Would there be general conversations about



1 the state of the financial system, specifically the
2 bond market?

3 MR. ELY: There would be general conferences
4 on the state of the market and they would certainly
5 probably not pinpoint a specific issue at a specific
6 price but the Committee could certainly give advice
7 to the federal government on how much, what terms,
8 what terms in matters of price -- they could give
9 them amounts, price and maturities that would
10 allow the government to choose which issues they
11 would be wise to finance in and without disclosing
12 the exact issue to the committee who should not
13 have that knowledge.

14 COMMISSIONER GIBSON: Suppose that there
15 were considerable differences of view amongst the
16 men?

17 MR. MILNER: That, Mr. Gibson, is the
18 reason we think there should be a committee. We
19 believe that the present system which is used today
20 by the Bank of Canada in consulting, if you like --
21 a dozen different dealers individually, we believe
22 that collectively three or four people could give
23 far better advice around a table than with the advice
24 you get from six or seven individuals.

25 MR. ELY: Might I enlarge on that by
26 saying that you would be surprised to find in a so-
27 called steering committee on a provincial issue that
28 there has never been to my knowledge a considerable
29 divergency of opinion, never. It is amazing how
30 accurately that kind of a committee can measure various



1 areas of the market both as to volume and price.

2 COMMISSIONER GIBSON: But would not a
3 discussion of this kind reveal to you what the
4 government had in mind?

5 MR. ELY: If it was held quarterly then
6 it would have no significance on when the government
7 might come to the market. If it was held immediately
8 prior to the government issue and it was obvious
9 that it would have to refund that issue because it
10 did not have enough working capital, then I think
11 the discussions should take place on such a plane
12 that it would not be disclosed to those people in
13 what area they were going to do their financing.

14 MR. WADDS: Could I say something? In
15 the United States this committee is called in
16 Washington prior to every major piece of financing
17 that the government does. As you know, there has
18 never been any question of a leak of information,
19 and what goes on at those meetings I have no idea and
20 I do not think anybody else has, except the people
21 that go to them and I think that system could work
22 quite effectively here. This, for the record, is
23 another attempt which we would like to make to develop
24 a better liaison between the issuing body and the
25 ultimate buyer and we are in touch with all the people
26 who buy securities and this would make it simple
27 for the Department of Finance to cover this type
28 of knowledge with the people in the field. I think
29 it would be very useful.

30 COMMISSIONER HARROLD: You make certain



1 recommendations concerning the Board of Directors of
2 the Bank of Canada in recommendations numbers 21 and
3 22 on page 6. The first question would be, would
4 you not think if these recommendations were carried
5 out, that at this executive committee would have
6 approximately the same kind of advice to offer as
7 you would get from the committee that you are
8 suggesting for the Department of Finance.

9 MR. BEATTY: Mr. Cox, would you speak
10 on that, for a minute?

11 MR. COX: I think, sir, the problem
12 has been that the appointment of directors to the
13 Bank of Canada have become a little too political
14 and they are not necessarily chosen on the basis
15 of their education, the kind of work they do, and
16 there is the specific exclusion of bankers, which
17 is not the case in the Bank of England or the federal
18 reserve, and it seems that if the Board is to be
19 of any help to the Governor and his senior personnel
20 in arriving at policy decisions, it would be considerably
21 better if these men did have a financial background,
22 either educationally or from the type of work they do.

23 COMMISSIONER HARROLD: That meets
24 with your suggestion in Section C.19 in which you
25 say "useful guidance".

26 MR. COX: Yes. I have never attended
27 one of the meetings and I do not know what goes on,
28 but there are so few people who would appear to be
29 able to have sufficient knowledge to give any advice
30 or guidance to the Governor on what was a pretty highly



1 technical field.

2 It may be that people will advise him
3 on how business conditions are in the provinces
4 which they come from, or what the outlook is for
5 the potato crop, or something like that; this is
6 important, but it will not help the banks in arriving
7 at a policy that will fit the needs of the economic
8 situation at the time.

9 COMMISSIONER HARROLD: I agree there
10 are times when potatoes may be important, but as
11 to the number you have there, would you change the
12 number from the present twelve?

13 MR. COX: That is something I had not
14 thought about. It seems enough, does it not?

15 MR. ELY: Are there twelve?

16 MR. COX: There are twelve now, I believe.

17 MR. ELY: I think that is right. I do
18 not think this is a question of having a large number,
19 I think it is a question of having a board that are
20 skilled to give the Governor advice and now it seems
21 as though they are chosen regionally rather than
22 for ability. I do not mean they have not got ability,
23 but they are chosen regionally by provinces but it
24 might be better if they were to have them all come
25 from two or three provinces and they can find the
26 right men. The men are available.

27 COMMISSIONER HARROLD: But are they not
28 to be from diversified occupations even if they do
29 come from the different provinces?
30



1 MR. ELY: It seems as though there is
2 a certain number per province, but no matter; certainly
3 if the Act reads that they come from diversified
4 industries perhaps that is a worthy reason, but
5 I think they could probably find a better answer
6 to that by making it a man with knowledge of financial
7 affairs in the country so that they could get better
8 advice for the bank.

9 COMMISSIONER HARROLD: How long has the
10 change in personnel, then -- you suggest that the
11 directors would have more control than they have
12 at the present time, or do you still suggest that
13 the Governor would have the power to control?

14 MR. MILNER: Mr. Harrold, I do not think
15 you can ever have a central bank operate without a
16 governor having the power of veto, but he would be
17 so subject to advice that you would question whether
18 the power of veto would ever occur. It is really
19 the same recommendation as we have got for the advice
20 on the issuance of new securities. In other words,
21 that there is somebody to consult outside his own
22 immediate circle who would be competent to give them
23 better advice than they are getting now under existing
24 circumstances. I could not conceive of the executive
25 committee of the Bank of Canada meeting -- we suggest
26 that they meet fortnightly.

27 COMMISSIONER HARROLD: Do you know how
28 often they meet now?

29 MR. HARRIS: I think it is eight times
30 a year.



1 COMMISSIONER HARROLD: The executives?

2 MR. MILNER: The executive committee
3 is only one man -- oh, are there two now?

4 MR. WADDS: The deputy minister and one
5 director, I believe.

6 COMMISSIONER HARROLD: You would not
7 find included officials and directors of banks,
8 chartered banks or employees?

9 MR. COX: I do not know why we should.

10 MR. MILNER: We do not believe that -- we
11 are trying to get away from anything political in
12 so far as banking is concerned, and the calibre of
13 person who has risen to the rank of general manager
14 or bank's president or president of a bank, or
15 important industrial people are beyond politics,
16 in our view. We think in this way we would have
17 an impartial opinion of what they think is good for
18 the country, if you have the right people on the board
19 and I think to exclude the chartered banks'
20 representatives would be fatal. It would be
21 fatal not to include them in that category.

22 COMMISSIONER GIBSON: Mr. Milner, how
23 could you just envisage a group of people like this;
24 some skilled investment dealers and bankers talking
25 about things that in any event might not accommodate
26 their own interests. How would you do this? That
27 is, if they are still fully occupied in their regular
28 jobs?

29 MR. MILNER: It has worked in other
30 countries, Mr. Gibson.



1 MR. SHAW: Well, in the present system
2 is it not true that some of the existing or preceding
3 governors have been connected with business enter-
4 prises where the same concern might not have arisen?

5 COMMISSIONER HARROLD: There was a case
6 of central bank officers and the senior top officers
7 coming from other groups where their interests are
8 conflicting with the central bank and they are acting
9 as advisors to the Governor of the central bank.



1 MR. SHAW: My question was, going back over
2 the past directors, isn't the case that we could find
3 amongst those people people who, if we retraced their
4 business connections, where you would find the decisions
5 made by that board could have a serious impact or
6 effect upon the businesses with which they were connected,
7 and yet that has not precluded them from being on the
8 board before.

9 COMMISSIONER GIBSON: I don't think you would
10 find any bankers or investment dealers.

11 MR. WADDS: You will find a senior director
12 of an insurance company who is a director, where there
13 could have been an effect by the bank's action.

14 MR. HARRIS: The Bank of England, the directors
15 there are merchant bankers and commercial bankers to
16 a large degree, and there was an enquiry some time
17 ago, and it came out there was no problem at all.

18 COMMISSIONER BROWN: Except they do not have
19 anybody from the clearing banks. They are all from the
20 smaller institutions.

21 MR. HARRIS: Merchant banks.

22 COMMISSIONER BROWN: Yes, merchant banks.

23 THE CHAIRMAN: What about the Federal Reserve?
24 They are all full-time directors there.

25 MR. COX: Each of the twelve district federal
26 reserve banks has three classes of directors: Two of
27 those three classes are chosen from bankers in the area
28 in which the particular bank has jurisdiction, and the
29 presidents of all those banks form the board; the
30 board of governors of the Federal Reserve system is



1 selected from these twelve.

2 THE CHAIRMAN: The Board of the Governors
3 of the Federal Reserve are full-time governors?

4 MR. COX: Yes.

5 THE CHAIRMAN: They are not carrying on any of
6 their former business; they cut adrift from their
7 former business associations?

8 MR. COX: But that is not true of the directors
9 of the District Federal Reserve banks.

10 THE CHAIRMAN: Oh, no. The policy is directed
11 from the board of governors.

12 MR. COX: Yes, but they get their information
13 from bankers.

14 THE CHAIRMAN: I have often wondered why
15 it is necessary to exclude certain segments of the
16 business community who probably know more about the
17 problems involved than anybody else just because there
18 might be conceivably a conflict of interests. Business
19 is full of conflicts of interest. Directors of banks
20 have frequently conflicts of interest between their
21 business, but they have to go outside the door and pretend
22 they don't know anything about it. In all corporate
23 business, directors frequently have conflicts of interest
24 and they simply have to declare their interests and
25 refrain from voting, if it involves a conflict. But,
26 it seems to me -- and I am just thinking aloud here --
27 if you gentlemen have any opinion to express as to broadening
28 the field from which directors of the central bank can
29 be drawn so that there would be a much greater infusion
30 of highly qualified people in this particular field.



1 MR. COX: That is what we feel.

2 THE CHAIRMAN: As well as having representatives
3 from other lines of business, because that also is very
4 important, but at the present time there is complete
5 exclusion of anybody who is really qualified in the
6 field unless he happens to be a retired banker. I think
7 there is a great loss there, myself.

8 MR. ELY: I think we as an industry feel that
9 too.

10 COMMISSIONER HARROLD: Have you gone so far as
11 to suggest there should be full-time directors?

12 MR. MILNER: Not in our brief, we haven't.

13 COMMISSIONER HARROLD: I should have put it in
14 the form of a question.

15 MR. COX: I think I would like to think about
16 that one. I don't know whether it is necessary to have
17 all full-time attend the meetings with the Department
18 of Finance or the Bank of Canada. It might not be
19 necessary, unless possibly the executive committee
20 might be represented by a full-time person.

21 MR. ELY: A full-time director would immediately
22 lose his usefulness by not working on anything else.

23 MR. SHAW: Some of his usefulness.

24 MR. ELY: Some of his usefulness, yes, that is
25 better.

26 COMMISSIONER GIBSON: The problem here is that
27 we get the impression from your memoranda and
28 recommendations that you would like to have a more
29 active board that would take a more aggressive part
30 in formulating monetary policy. In other words, not a



1 board of directors that pass on the more or less corporate
2 things that go through, but a board that is actively
3 engaged in thinking about and formulating monetary
4 policy. This is why I raised the question of conflict
5 of interest. If it is the kind of board which functions
6 the way the present board does, it does not appear the
7 conflict will be serious, and in the Bank of England
8 they do discuss these things -- some of the things where
9 conflicts might arise don't get to this type of director.
10 It is this question I am really thinking of.

11 MR.COX: I think our thinking is that any
12 conflict of interest that might arise seems to be
13 less serious than the Governor of the Bank lacking
14 advice that might be useful to him.

15 MR. SHAW: Or some body on which he could
16 try out his proposal; that would be the function, it
17 would seem to me, the board would best serve. It would
18 provide a body of knowledgeable people to whom the
19 Governor could take the ideas he has formulated, and
20 I would not see this as ideas originating within the
21 board. They should still originate with the active
22 governor and he in turn has someone to whom he could
23 take these suggestions and work them over a bit before
24 they become policy.

25 COMMISSIONER BROWN: What sort of decisions
26 do you visualize being made?

27 MR. SHAW: I am thinking of changes in monetary
28 measures that are being introduced. I think the decisions
29 would be as to the measures themselves and as to the
30 timing of them.



1 MR. COX: You get a practical opinion from
2 somebody who is perhaps going to be affected by some
3 of these changes as to what the effects are going
4 to be.

5 COMMISSIONER GIBSON: Bearing in mind monetary
6 policy is most of the time more of a flow than a series
7 of disjointed and separate decisions, do you think
8 this is really feasible? When you have a crisis you
9 sit down and decide and make some very definite decisions,
10 but most of the time isn't it a matter of guiding something--
11 moving a little this way and that way and feeling your
12 way along, and in those circumstances can you use this
13 kind of advice?

14 MR. BEATTY: Could not that crisis be avoided
15 with proper outside assistance?

16 MR. MILNER: Put it another way, Mr. Gibson:
17 Could not the Governor go to the government and say
18 the advice of his executive is rather contrary to what
19 the government opinion had in mind. I think you would
20 accomplish a tremendous amount if you had the really
21 top calibre of people in this country advising the
22 central bank. I cannot help but feel it would be a
23 constructive measure in the future of the country.

24 COMMISSIONER HARROLD: You see no need for
25 any geographical or industry representation on this
26 kind of board; is that right?

27 MR. MILNER: Well, Mr. Harrold, I think in
28 picking a board -- of course, it is very difficult to
29 pick a board, obviously -- but all that we put in our
30 brief, or that we suggested, is that it be completely



1 divorced from a political board and completely divorced
2 from a regional board; that is, not to have it
3 automatically with somebody from New Brunswick, Manitoba,
4 Saskatchewan and two from Ontario and so on. It would be
5 picked by the manpower or the man ability/^{rather}than regional --
6 diversity of interest.

7 MR. COX: They should not all be bankers or
8 all economists or all dealers.

9 MR. LEMAN: Mr. Gibson, if the inference is
10 that it may not be desirable to have people with knowledge
11 and experience in matters of finance and banking on
12 the board of the Bank of Canada to advise the Governor,
13 why have a board at all?

14 COMMISSIONER GIBSON: Well, we are asking you.
15 I don't know.

16 COMMISSIONER BROWN: I think we should also
17 say that I do not think at any stage has there been an
18 inference that you should not have people with this
19 experience and knowledge. There is an inference you
20 should not place people, particularly people who have
21 directly and obviously a conflict of interest in that
22 position. I don't think there is any inference that
23 type of person is not wanted.

24 COMMISSIONER GIBSON: There is no inference
25 at all. This is the kind of problem that could arise,
26 and we are trying to get your view.

27 MR. MILNER: I think we have said everything
28 we have in mind.

29 COMMISSIONER HARROLD: In selecting this type
30 of board what would be the end result -- where would they



1 come from? The financial community?

2 MR. MILNER: I would think, Mr. Harrold, that
3 the prime people I would visualize, if you are talking
4 of a board, let us say, of ten people, to use a number --
5 I would think you would want to get as much diversification
6 as possible. You would want a banker, but industry
7 would be the prime people that you would employ on the
8 board. I think industry would rank the highest --
9 financial institutions: Put it on that basis.

10 --- Short recess.

11 THE CHAIRMAN: We will now resume.

12 COMMISSIONER GIBSON: Mr. Chairman, I would
13 like to ask a question or so about moral suasion. You
14 have made it clear to us, gentlemen, or some of you have,
15 that you don't like moral suasion as a long-term operation.
16 What do you think of the use of this instrument -- perhaps
17 we should not even call it moral suasion. We will just
18 call it "persuasion", and that would perhaps be more
19 realistic. What do you think of the use of this
20 kind of an implement in monetary policy? I understand
21 from time to time you have encountered persuasion --
22 moral suasion. We would like to know whether you
23 feel it is an effective instrument in monetary policy
24 and whether it can be used too frequently, and so on?

25 MR. COX: I think it is highly desirable that
26 the bank can make use of this kind of technique because
27 I think it would be almost impossible to visualize an
28 act for the bank which would cover all the things and
29 all the contingencies that might arise from any sort of
30 external or internal pressures. We have set out quite a



1 bit on what we know that the bank has done in this
2 field, and it covers a pretty wide area, but I think
3 it is very important that it should be made clear that
4 short periods should be involved, and when the persuasion
5 as such has served its purpose that whatever instructions,
6 or whatever you want to call them, the Governor has
7 issued to those concerned, that they be advised this
8 emergency is now over and whatever they have been doing
9 has served its purpose.

10 COMMISSIONER GIBSON: Do you feel it applies
11 only to emergencies?

12 MR. COX: No, not necessarily emergencies;
13 that is probably a bad word. It might be better to say,
14 situations that require some sort of action.

15 COMMISSIONER GIBSON: Any sort of situation,
16 or does it need to be a fairly serious one?

17 MR. COX: It depends on extent, I suppose, but
18 I think it is desirable that the bank be able to
19 go to some group who have some sort of control over
20 some kind of credit and say, "You are overdoing it.
21 Can you change your policy a little. This is not in
22 the best interests of the country." I think, carrying
23 it a step further, it may be interesting to pursue
24 the thought that we have now had quite a few experiences
25 of the use of moral suasion, and is there anything there
26 that should be enacted that the bank should have legislative
27 power over? For instance, reserves for near banks or
28 terms of credit extension by finance companies, and
29 what not. I would think perhaps this would be something
30 that you would be looking into in your deliberations



1 later.

2 COMMISSIONER GIBSON: We will be glad to have
3 your views.

4 MR. COX: I don't know that I am qualified
5 to express any views as to whether the bank should have
6 powers over anything specific in this area, but it is
7 rather interesting that the Federal Reserve seems to
8 have a number of these powers. On the other hand,
9 the Bank of England seems to rely directly on moral
10 suasion and does not seem to feel it needs an enactment.
11 I don't know whether that represents the material
12 of the market in which they are operating.

13 COMMISSIONER GIBSON: Are there any limits ,
14 apart from the time limit, that you feel ought to be
15 applied to this technique?

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1 You said earlier that you think if a thing goes on
2 a long time it ought to be put in legislation. You
3 said that in the context of the secondary reserve

4 MR. COX: What would you mean by limiting,
5 Mr. Gibson?

6 COMMISSIONER GIBSON: Well, again I am
7 not expressing an opinion; I am trying to create
8 a situation that you can comment on. When some-
9 body wants you to do something that you can see
10 will be very much against your interests and you
11 are the people who are asked to do this, some may
12 do it and some may not. If it is just a little
13 against your interests or if you can all agree that
14 this is good in the national interest, does this
15 problem arise to the same degree?

16 MR. COX: I think it would be most
17 important that the governor's prestige is such
18 that he could go to a group and present a con-
19 vincing story and be successful in his efforts
20 to persuade them to change their tactics. This,
21 perhaps, raises the question that if he is going
22 around every week asking people to do something
23 perhaps he is overdoing it.

24 COMMISSIONER GIBSON: How far do you
25 think he should go in asking people to go against
26 what they conceive to be their self interest?

27 MR. COX: I think that would have to
28 be his decision. This is something of an individual
29 judgment, is it not?
30



1 COMMISSIONER GIBSON: Yes, but it is
2 an important question.

3 MR. COX: It would have to be in the national
4 interest, there is no doubt about that.

5 COMMISSIONER GIBSON: Clearly in the
6 national interest?

7 MR. COX: I think pretty clearly.

8 COMMISSIONER GIBSON: So that nobody
9 would recognize this?

10 MR. COX: Or it could be explained to
11 them in such a way -- but I do not think he should
12 threaten some sort of action to gain his ends.

13 THE CHAIRMAN: When you talk about
14 persuasion or moral suasion it is really not that
15 at all. In the background there is, although
16 perhaps not in the open, an implicit possibility
17 of a threat when the Governor of the Bank of Canada
18 asks the chartered banks to do certain things at
19 a certain time, is that not right?

20 COMMISSIONER GIBSON: Mr. Chairman, I
21 was talking about this in the context of the relation
22 between the Bank of Canada and the Investment Dealers.

23 MR. COX: Possibly there is, Mr. Porter.

24 THE CHAIRMAN: If the Governor of the
25 Bank of Canada felt strongly enough about it and
26 was determined that his proposal should be brought
27 about he would be in a very strong position to go
28 to the government and ask for necessary legislation
29 and they all know that. The governor is not likely
30 to ask for something of that kind unless he has good



1 reason from the national standpoint to do it. I would
2 think it is not just a voluntary act on the part of
3 the parties that are approached whether they are
4 investment dealers or banks or whoever they may be.

5 MR.COX: Well, of course, this raises
6 the point whether this threat of legislation would
7 be desirable for the country on a permanent basis.

8 THE CHAIRMAN: Well, there is always
9 that in the background. There is always the possible
10 legislation. Very often people want to avoid that.
11 They would rather comply with the suggestion for the
12 time being in the hopes that perhaps in time conditions
13 would change and it would be lifted?

14 MR. COX: Well, actually the way I was
15 thinking of it is that he should go to the banks and
16 say: "Look, you do this or I will change your cash
17 reserves" or something. That is the kind of threat
18 I was thinking of.

19 THE CHAIRMAN: No, he does not have to
20 make a threat. No doubt he has very persuasive
21 arguments but there is something always in the back-
22 ground and especially when matters emerge in which
23 there is a national interest involved and people are
24 approached most of them will accept the views of
25 authorities that there is some national interest
26 involved. If one individual decides to disobey the
27 situation he knows perfectly well that something will
28 happen.

29 MR. BEATTY: Not necessarily. In the
30 case of the finance companies controlled from outside



1 of Canada I believe there was an instance where they
2 did not co-operate and nothing was done.

3 COMMISSIONER BROWN: I think this clears
4 up the point that unless there is some club hanging
5 in the cupboard in the background it is more difficult
6 for moral suasion to be effective?

7 COMMISSIONER GIBSON: I do think there
8 are circumstances, Mr. Chairman, where different groups
9 will recognize the national interest. I am sure
10 the investment dealers would agree with anything that
11 was suggested that might be in the national interest --
12 similarly with the banks, although there is the
13 possibility of the use of power always there. I was
14 just trying to get some idea of the ranges of this.
15 The sort of impression I gathered from you was that
16 it is not something continuing. You say partly in
17 the nature of an emergency you think moral suasion
18 is a good thing?

19 MR. COX: Yes.

20 COMMISSIONER GIBSON: And apart from that
21 you do not?

22 MR. COX: That is right.

23 COMMISSIONER GIBSON: Do you run into this
24 conflict of interest on moral suasion where some
25 people will come in and adopt suggestions and others
26 have not?

27 MR. COX: Not at first hand.

28 COMMISSIONER GIBSON: I mean in your industry?

29 MR. COX: Oh, I think we have. We have
30



1 definitely run into it in the case of the finance
2 companies somebody mentioned.

3 MR. MILNER: We have had it also, Mr. Gibson,
4 in our industry which comprises 190 odd dealers where
5 we have been requested on a moral suasion basis to a
6 very limited number of our members and the viewpoint
7 of the government was, I assume quite correctly, that
8 if you ever tried to publicize it to 191 people it
9 would not work. You might as well make an act of
10 it so that they get two, three, half a dozen people
11 who were the most important people in that particular
12 field but that did not prevent the 186 others from
13 carrying on their normal transactions and I do not
14 think any one of the people involved had any thought
15 that they were not doing the right thing by taking
16 the suggestion of the central bank if they did not
17 do a certain transaction.

18 COMMISSIONER GIBSON: Perhaps another way
19 of looking at this thing would be to ask you whether
20 or not you are in favour of the use of directives and
21 controls by the central bank if that is related to
22 the question of moral suasion. This is sometimes
23 an alternative.

24 MR. MILNER: Well, I can answer that, I
25 think, without any difficulty. We would much prefer
26 moral suasion than having direct control. We do
27 not like controls if it is humanly possible to avoid
28 them whether from the central bank or any other source.
29 I believe our freedom of action in being left to our
30 own judgment is far better than having legislation



1 which is so difficult to take off. Once it is on it
2 tends to remain. Moral suasion is a far better method
3 of accomplishing what the central bank may want.

4 COMMISSIONER GIBSON: I am thinking of
5 selected credit controls actually.

6 COMMISSIONER BROWN: Such as the suggestion
7 on page 27 of Section C.

8 MR. COX: This is a question of margin
9 requirements in that case, sir. I think I would agree
10 with Mr. Milner that if the Governor feels that some-
11 thing needs changing along the line of these examples,
12 if he is able to do it through moral suasion that is
13 perhaps better than giving him legislative powers.

14 COMMISSIONER GIBSON: You would rather do
15 it informally than formally?

16 MR. COX: Yes.

17 COMMISSIONER GIBSON: Would you still say
18 that if it would be a continuing problem?

19 MR. COX: Well, if it is a continuing
20 problem then I think it becomes a question of legislation.

21 COMMISSIONER BROWN: I would just like one
22 or two more fairly quick questions if I could get an
23 answer. And this is in connection with the bill market.
24 I wonder for the record if someone would care to outline
25 the nature of the undertakings that are taken by the
26 14 members of the money market. What obligations do
27 you undertake in exchange for this right?

28 MR. HARRIS: Tendering for treasury bills?

29 COMMISSIONER BROWN: No, anyone can tender
30 on bills.



1 MR. HARRIS: No, a prime distributor cannot
2 tender. You mean lines of credit?

3 COMMISSIONER BROWN: Yes.

4 MR. HARRIS: Well, the 14 lines of credit
5 are in the central bank. They are given these lines
6 first of all because they are dealers who have shown
7 in the past that they are active and able to distribute
8 enough obligations and have shown a responsibility. They
9 have got the capital that allows them to participate
10 in the money market. The money market men must have
11 quite a bit of capital. I do not know if all terms
12 given under the Bank of Canada are in the same form
13 or not. The Bank of Canada has a pretty good idea
14 of each firm's financial responsibility and I think
15 the firms which have the privilege of rediscounting
16 money market securities at the Bank of Canada realize
17 this privilege and react accordingly and participate
18 very actively in placing government securities. Is
19 there anything more?

20 COMMISSIONER BROWN: Is there any obligation
21 in connection with the treasury bill tenders?

22 MR. HARRIS: The actual bill tenders? There
23 was a little while ago a moral suasion directive --
24 this is what you are after, I gather -- it was done
25 in a very informal way. The dealers were allowed
26 to tender for not less than 10 per cent of the
27 treasury bills and not more than 25 per cent of the
28 bills each week. This was to try and create some
29 stability in the treasury bill market. Some directives,
30



1 I think, have been done more formally through letters
2 to the firms with regard to the item we mentioned
3 earlier for the dealer's line of discounting their
4 bank rate from the chartered banks. This was going
5 through the formal channel. This other was not.
6 It was informal through a meeting with the money
7 market traders and not with the senior heads of the
8 firms, I believe, at that time.

9 Most firms have more or less abided by
10 the not over 25 per cent, but recently I think in
11 this crisis the 10 per cent has not been a very
12 practical thing. People have bid for 10 per cent
13 but some of the bids would be a way out of line. I
14 think the bids are usually put in and scaled so that
15 the bids are not very attractive. Does this answer
16 the question?

17 COMMISSIONER BROWN: That is what I wanted.

18 MR. MILNER: The only other question, Mr.
19 Brown, on that is that the 14 members report weekly
20 to the Bank of Canada their position on the short term
21 securities.

22 COMMISSIONER BROWN: I would like to bring
23 out one other point and that is: is there a presumption
24 that if somebody who is not now in that market wishes
25 to develop an interest in this that he can become one
26 of the money market group?

27 MR. HARRIS: The money market dealers, there
28 has been quite a change over the years. Recently one
29 firm joined during the last year and it seems to be
30



1 quite a flexible organization. This is up to the
2 Bank of Canada and not the I.D.A. but it seems to
3 be quite flexible and there have been many changes
4 within the money market since its inception.

5 COMMISSIONER MACKINTOSH: I just wanted
6 to add one point. Is there any suggestion of influencing
7 your inventory through the short term money market
8 instrument that you hold?

9 MR. MILNER: None whatsoever.

10 COMMISSIONER BROWN: On bankers' acceptances
11 which I suppose we might say are almost stillborn.

12 MR. HARRIS: Well, about two week's life.
13 They were introduced in theory June 9th at which time
14 theoretically a person using an acceptance could
15 borrow 5 per cent as against a primary of $5\frac{1}{2}$ per cent
16 and in theory now the acceptance is $6\text{-}3/4$, $6\text{-}7/8$
17 compared with a primary of 6 per cent. At the moment
18 nothing has happened.

19 COMMISSIONER BROWN: The only question I
20 was going to ask is, have you any comments on the
21 \$200,000 size?

22 MR. HARRIS: Well, from my several weeks
23 of study and my personal point of view I found some
24 of the people who were interested in acceptances were
25 interested in amounts less than that size. I think
26 the type of formula that they use an acceptance market
27 for might be less than that. Acceptances are
28 designed for self liquidating financing, warehousing
29 and trades, and where in a single instance it is much
30 more possible you want it over a period of time and



1 not on a particular day.

2 COMMISSIONER BROWN: What do you suggest
3 would be more acceptable than the \$200,000?

4 MR. HARRIS: Well, certainly \$100,000 would
5 bring more people into it. I think there is a problem
6 of both the banks and the dealers on the paper work
7 involved and I think \$100,000 would be much more
8 practical.

9 COMMISSIONER BROWN: One question on corporate
10 paper and finance company paper. In June 1938 the comment
11 was made that the dealer usually operates at a smaller
12 commission than he would on finance paper and at first
13 glance it seems a little odd because finance paper
14 is on tap whereas this is a one shot effort, and one
15 separate deal. Can you put on record why it is
16 a smaller commission?

17 MR. HARRIS: Well, this came up through
18 something we were discussing yesterday, competition
19 within the industry to a degree. Corporate paper
20 has indirect benefits to a dealer who conducts this
21 account.

22 COMMISSIONER BROWN: You are servicing the
23 account?

24 MR. HARRIS: You are servicing the account,
25 you are doing a job for him, you are helping people
26 you have long done financing for. You are in
27 competition and dealing with firms that you have not
28 had contact with so it has resulted over the past
29 several years that the commissions usually have an
30 edge on a permanent basis rather than finance paper.



1 COMMISSIONER BROWN: It is in the nature
2 of a loss leader?

3 MR. HARRIS: No, I would not say that. If
4 the volume was large enough during the year to make
5 money on there is no problem there. Some of the
6 demand paper is -- also I think the reason that is
7 a loss leader it is only one firm and short term
8 obligations. Those people at other times would be
9 buying Canadas short term, they will not be buying
10 finance paper on provincial obligations.
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1 At one particular point they may want finance papers,
2 and at other times they may want other obligations, and
3 you have to service them in all fields, I think.

4 COMMISSIONER MACKINTOSH: I have one question
5 that refers back to yesterday's discussion largely
6 in respect to corporate securities. I would like to
7 put this question in order to clear up the views that
8 were expressed at that time.

9 Mr. Milner, would you think that the association,
10 or a considerable proportion of its members would favour
11 regulations under legislation of full and continuing
12 disclosure as that is commonly understood by all the
13 corporations issuing debtor and equity securities to the
14 public?

15 MR. MILNER: Well, Dr. Mackintosh, we have had
16 some discussions along that line of thought. A few
17 of us have taken a look at the requirements of the
18 New York Stock Exchange both as to listing and, more so,
19 on continuous disclosure, and again in respect of
20 certain of the facts we were gathering, such as takeover
21 bonds, voting stocks and various other restrictions.
22 It seems to me, speaking personally, that in Canada with
23 only nine provinces instead of -- I don't know how
24 many there are now; 51 or 52, or something like that.

25 COMMISSIONER MACKINTOSH: There are now 10
26 in Canada.

27 MR. MILNER: I was getting the banks mixed
28 up. With only 10 provinces, four provinces having
29 practically identical securities regulations, that it
30 would be well to consider such a system. How this could



1 be done legally I do not know. Whether this would
2 necessitate federal legislation or whether you would
3 have to have the combination of federal legislation
4 and, using our old term, moral suasion with the provinces
5 to change the regulations in respect to full disclosure
6 and, more particularly, perpetual full disclosure annually
7 on all securities that are held by the public, I do not
8 know. It would start very simply with the three major
9 stock exchanges. If the three major stock exchanges
10 had, for instance, identical listing requirements that
11 could not be varied to suit certain circumstances and ,
12 at the same time, if it were obligatory to publish
13 quarterly earnings statements or, at the worst, half
14 yearly earnings statements and annually to publish
15 a proper digest of the operations of the company --
16 this is outside of their normal balance sheets that
17 are issued -- so that the public could be informed
18 as to what security it owned, whether it be a bond,
19 a debenture or common stock, all carried to that extreme,
20 and if the legislation governing the listings were
21 made adequate, along with completely adequate provincial
22 legislation providing that every company that had
23 public shareholders would be forced to abide by the
24 same set of rules, I think it would be the greatest
25 step forward that could be taken, both for the protection
26 of the public in the true sense of the word but, even
27 more so, to strengthening the viewpoint of outside
28 people -- that is non-resident people who would have
29 a far better picture of our industrial development if
30 such information were available. I do not know how it



1 could be done legally. We are completely at sea as
2 to whether the securities acts could be superimposed
3 from Ottawa, or whether they could not, but I would
4 assume that for instance the Companies Act, which is
5 federal legislation, actually has certain of these
6 restrictions in it, but they have never been enforced
7 and can only be enforced if somebody complains. Of
8 course, the chances of an individual shareholder
9 complaining are so negligible that companies are able
10 to avoid disclosure in the normal course of events.
11 I refer to full disclosure of course. I am sure that
12 every one of our members would be in favour of the fullest
13 disclosure that is possible, but I would like to have
14 a couple of other people, if you do not mind, sir,
15 make a few remarks in this regard.

16 COMMISSIONER MACKINTOSH: Let me interject
17 here. At this point I am not interested in discussing
18 whether you would do this by amending the Companies
19 Act or by separate legislation, or what the technique
20 would be. That would be a later thing. I am not
21 interested at this point in your methods of enforcing
22 this. I would like to clear in my own mind the question
23 as to whether this group would feel that if this could
24 be accomplished it would be a good thing and would
25 support them in their various associations in carrying
26 out what they think is proper.

27 MR. MILNER: Dr. Mackintosh, I was only speaking
28 in this particular instance not as Chairman of this
29 brief committee, but as an individual.

30 I would like to ask Mr. Beatty, if I may, if he



1 agrees with my premise. He could take it up at the
2 association level and we could get you a very definite
3 answer within a very short time.

4 COMMISSIONER MACKINTOSH: Fine.

5 MR. BEATTY: I feel confident that the members
6 of the association would approve more complete disclosure
7 if we can arrange it. I do not think it needs to be
8 taken up at the association level.

9 MR. STRATHY: Dr. Mackintosh, perhaps this
10 is a personal view as the result of vast experience
11 which I have had in connection with the stock exchanges
12 and I do not know whether you would like that, but I
13 know that for the last number of years stock exchanges
14 generally have hoped that there would be a method found
15 whereby they could regulate their listing companies ,
16 and that full disclosure be defined in respect of
17 listing stocks.

18 There has been a very difficult situation
19 develop through the different rules that prevail on
20 different stock exchanges. I am sure the will is there.
21 Perhaps that gives a little broader viewpoint than
22 just expressed by the I.D.A.

23 COMMISSIONER MACKINTOSH: Thank you.

24 Could I ask another question? I do not want
25 to pursue this, but you are satisfied that while nobody
26 could probably define literally what you call full
27 disclosure, and someone a moment ago gave a more full
28 description, you do feel that practically for the
29 purpose of the regulations an acceptable definition
30 of what would be full disclosure could be arrived at?



1 MR. STRATHY: I am sure it could be worked out.

2 COMMISSIONER MACKINTOSH: It could be arrived
3 at?

4 MR. STRATHY: I am sure it could be worked
5 out to the benefit and satisfaction of the requirements
6 of the shareholders, giving them that information which
7 I feel a lot of them think they should have.

8 COMMISSIONER MACKINTOSH: That satisfies my
9 requirements, thank you.

10 THE CHAIRMAN: Would you be in a position to
11 work out a definition of that kind which you would
12 agree to as being adequate for the purposes? Would
13 you be able to do that?

14 MR. STRATHY: I think it could be worked out.

15 THE CHAIRMAN: I do not mean right now. I mean,
16 in due course perhaps you could send one to us that
17 you think would be an adequate definition.

18 MR. STRATHY: I am quite sure it could be
19 worked out. I am not sure whether it is within the
20 prerogative of the stock exchanges, or whether it is
21 perhaps a joint thing..

22 THE CHAIRMAN: I am not interested particularly
23 in who does it.

24 MR. STRATHY: It could be worked out.

25 THE CHAIRMAN: Since you are before us and
26 you have made this submission as to your views on the
27 whole subject, perhaps you could produce a definition
28 which satisfies you and the stock exchanges or anyone
29 else you may feel should be consulted. Such a definition
30 would help us.



1 MR. BEATTY: The mortgage people should be
2 consulted.

3 THE CHAIRMAN: That is entirely up to you.
4 If you could send such a definition in due course, and
5 there is no great hurry about it, it would be of great
6 assistance.

7 MR. BEATTY: We could consult with the exchanges.

8 MR. SHAW: This is the sort of question that
9 could be developed when you hear from the exchanges,
10 because it seems to me this is something that must be
11 developed between the exchanges, ourselves and others.

12 THE CHAIRMAN: You may keep this in mind and
13 in due course you will be in touch with us again, I am
14 sure, and you will be in touch with the exchanges.

15 MR. SHAW: Yes. The willingness is within
16 our association to co-operate.

17 THE CHAIRMAN: It is easier for you to do this, and
18 more satisfactory, than for us to do it.

19 COMMISSIONER MACKINTOSH: At any rate I am
20 sure the advice of the association is available to us.

21 THE CHAIRMAN: Yes.

22 COMMISSIONER LEMAN: Mr. Chairman, I have a
23 few loose ends to tie together. I would like to refer
24 the witnesses to paragraph 12 of Section E where the
25 point is made there in regard to corporate financing.

26 It is said in that paragraph that as shown
27 by Table 3 on page 5 small firms have relatively
28 more recourse to bank financing than the larger; debt
29 constitutes a smaller proportion of capitalization (and
30 much of the debt is represented by mortgages) and a



1 higher proportion of net profit is retained.

2 I am inclined to question that all these conclusions
3 flow from an examination of Table 3. For instance, in
4 respect to the retained earnings, which are about
5 equivalent to what you call surplus in that table,
6 except for the very small group of companies covered
7 under \$100,000 in total assets, the retained earnings
8 do not seem to me to show a very great tendency to
9 ascend with size. Would you agree with that?

10 MR. MILNER: Well, Mr. Leman, in answering
11 that question you must realize that the Royal Commission
12 on Finance has had a very tragic effect on the man that
13 wrote this document for us. He put his back out this
14 morning and is in bed. He has asked me to state that
15 this was prepared completely by himself and one other
16 firm in Montreal. I was wondering if it would be
17 possible to have that gentleman give us the words he
18 would like in answer, and we could submit this to you
19 in writing later.

20 COMMISSIONER LEMAN: I do not think we want
21 to make a big issue of it, Mr. Milner. I just wanted
22 to point out that that looked to be a strange situation.

23 MR. BEATTY: I think he is referring to the
24 source capital rather than the percentage earnings
25 that are retained. The retained earnings are a greater
26 proportion of the sources of capital available to these
27 smaller companies.

28 COMMISSIONER LEMAN: Well, as I say, it is
29 not a major issue.

30 I would like to go through these questions rather



1 fast because time is getting on.

2 There is a reference in Section E, paragraph
3 36 to the effect that private placements are becoming
4 more prevelant as time goes by. I suppose there is
5 statistical evidence to support this, but it does not
6 appear in the brief as far as I can tell. Would you
7 guess why that is?

8 MR. MILNER: The private placement method
9 of financing is cheaper in most instances than public
10 financing. In its instigation in Canada, and I am
11 speaking of in Canada particularly, some of our larger
12 insurance companies who, with their contacts with
13 various industrial concerns both large and small --
14 whether they approached the company or the company
15 approached them, I do not know -- have made the suggestion
16 through a dealer in all instances that if the dealer
17 would put these things togehter, they would be prepared
18 to advance the company the money that was required
19 under certain circumstances, and the dealer has drawn
20 up the trust deed, etc., and has been paid a fee for
21 such type of financing.

22 Mr. MacKeen brought this up in his remarks
23 before, that in bond financing of that kind it can be
24 quite costly over a period of years to the corporation.
25 It would not be at current interest rates, I hope,
26 but at other interest rates when it is lower, it does
27 become more expensive than previously. Your question
28 I assume was asked in respect of the cost of such
29 underwritings, and it is cheaper.

30 COMMISSIONER LEMAN: That was not quite my



1 last question. Why do you think it has become more
2 prevelant? Do you think it is because in general
3 the cost to the borrower is somewhat lower?

4 MR. MILNER: Yes.

5 COMMISSIONER LEMAN: Assuming that that is
6 so, the question stems from that: Do you think there
7 would be a good case to be made for a wholesale price
8 for corporate issues and a retail price, the two being
9 different?

10 MR. MILNER: Mr. Leman, our industry is
11 convinced that the proper method of selling securities
12 is at the same price for all investors. We have found
13 it has worked out far better to have one price only
14 rather than a wholesale and retail price. That applies
15 through the whole series of our operations both in
16 government bonds, provincial bonds and corporate bonds.

17 COMMISSIONER LEMAN: Therefore there is nothing
18 today against private placements if they are going to
19 take place?

20 MR. MILNER: No.

21 COMMISSIONER LEMAN: Yet in paragraph 38 B
22 you point to the reduced interest to insurance companies
23 for corporate bonds. Would you say that a reduced interest
24 on only/those bonds that are publicly offered is a good
25 thing, because you just said there was a trend toward
26 private placements?

27 MR. MILNER: Did you refer to paragraph 38 B,
28 sir, in Section E?

29 COMMISSIONER LEMAN: It appears at page 13 in
30 Section E; you say that the reduction in the leading role



1 of the insurance industry requires the investment
2 dealer to turn to several other sources. The
3 implication there is that there has been somewhat less
4 interest on the part of the insurance companies for
5 corporate bonds.

6 MR. WADDS: I would think that is a matter
7 of opinion, personally.

8 MR. MILNER: The answer to that, Mr. Leman,
9 is that in the last few years there has been quite a
10 marked change in the private placements mortgage
11 type of investment by our leading insurance and other
12 pension fund type of obligation, where they have financed
13 by means of direct mortgage rather than through the
14 bond route. This has cut down the amount of the public
15 financing particularly in the secondary corporations,
16 such as shopping centres and that type of instrument.
17 The shopping centres have been financed largely by
18 means of direct mortgages with insurance companies.

19 COMMISSIONER LEMAN: Those are lease-backs?

20 MR. MILNER: And are lease-backs.

21 COMMISSIONER LEMAN: As I say, I am going
22 through these rather quickly. I would just like some
23 simple answers.

24 In relation to paragraph 50 of Section E you
25 make the recommendation that the legislation be amended
26 so as to permit companies to deduct in arriving at
27 taxable income the actual cost of underwriting. Who
28 do you think that would benefit most, the operators
29 or the investment industry?
30



1 MR. MILNER: Mr. Shaw, would you like to
2 answer that?

3 MR. SHAW: Briefly, the borrowers.

4 MR. COX: However, it might make refundings
5 more frequent.

6 COMMISSIONER LEMAN: Well, if we might
7 jump now to 59 on page 21. You make reference there
8 to the fact that there are some things in the Canadian
9 Companies Act which tend to deter incorporation of
10 companies under its positions, and so on. What are
11 the features that draw people away from federal
12 incorporation?

13 MR. MILNER: There has been, I believe,
14 for about three years now -- there have been several
15 committees formed from the leading corporate legal
16 firms endeavouring to persuade the government to
17 amend the Companies Act to cover a lot of the situations
18 that are -- that they believe they could probably deal
19 with better than they are dealt with under the present
20 Act.

21 Take as an example the merger of a federal
22 company with a provincial company where you run into
23 the surplus situation. We put this into the brief
24 wanting to see if it was possible to have the Companies
25 Act looked into seriously for revision, but we do not
26 want to go into it in detail because we believe that
27 this is under corporate law and that is the place where
28 it should be dealt with. We did not deliberately --
29 we do not want to go into the details because it is
30 a thing that is beyond our ken.



1 COMMISSIONER LEMAN: You are not implying
2 it has a great effect on the matters we are discussing
3 here, the flow of opinions, and all that sort of thing?

4 MR. MILNER: Yes, it has an effect on
5 the flow of opinions. We think that a proper inter-
6 pretation of the Companies Act would assist in the
7 financing of industry.

8 MR. SHAW: And in particular where it
9 lists some of the things in the latter part of that
10 paragraph which we think should be revised.

11 COMMISSIONER LEMAN: Would you turn now
12 also quickly to paragraph J.9. You are referring
13 there to secondary distribution. The argument here
14 is to the effect that in the Canadian market the
15 commissions paid in this operation are double the
16 minimum stock exchange commission, whereas in the
17 States it ranges from four to $6\frac{1}{2}$ times the average
18 minimum commission rate. What is the base, what
19 is the minimum commission rate in both places?

20 MR. CRETZIANU: These are secondary dis-
21 tributions for which there are no set fixed commissions,
22 and the broker is at liberty to ask for whatever
23 commission he thinks the market will pay.

24 several of
In the United States/the secondary dis-
25 tributions, the majority of the secondary
26 distributions, have been done at substantially larger
27 spreads than in Canada. There have been many examples
28 of an overwhelming number of secondary distributions
29 at over four times the usual commission while in
30 Canada the secondary distributions are generally done



1 at the double commission.

2 COMMISSIONER LEMAN: But is the usual
3 commission lower than down there?

4 MR. CRETZIANU: No, the stock exchange
5 commission in the States does not differ very much
6 from the Canadian one. It might be a little lower
7 on certain kinds of stocks.

8 COMMISSIONER LEMAN: Well, elsewhere
9 there is a paragraph which tends to try to prove that
10 underwriting in Canada is not much more costly than
11 in the States, and here on the secondary distribution
12 it is your assertion it is less costly on the average
13 in Canada than in --

14 MR. CRETZIANU: Yes, it is a fact which
15 can be proved, that the commissions on secondary
16 distribution in the United States are substantially
17 higher than in Canada.

18 COMMISSIONER LEMAN: I would like to ask
19 you one more question. Going back for just a second
20 to the municipal financing, do you believe that a
21 municipal bond rating service in Canada would be of
22 great use to the industry and to the municipalities,
23 especially less known ones; if they knew that they
24 could make arrangements with a service to get themselves
25 rated?

26 MR. MILNER: Mr. Beatty, would you care to
27 speak to that?

28 MR. BEATTY: I believe it would be a useful
29 service.

30 COMMISSIONER LEMAN: Well, somebody has to pay



1 for the service. Do you believe it is viable?

2 MR. BEATTY: If it were such that it would
3 be obviously profitable, I believe there are several
4 organizations who would have undertaken it by now.

5 COMMISSIONER LEMAN: You do not believe
6 it would be viable?

7 MR. BEATTY: No, I do not believe it would
8 be profitable.

9 COMMISSIONER LEMAN: I would like now to
10 turn quickly to two sections on which I do not have
11 very many questions to ask, and one is the
12 risk capital section that you discuss in I, and
13 then small business financing in L. There is a
14 relationship there between the two. It shows what
15 is being done by the present sector and we have heard
16 from other people that it would be a good thing if the
17 I.D.B. were disassociated from the Bank of Canada.
18 Does the Association have an opinion on this score?

19 MR. MILNER: By being completely dis-
20 associated from the Bank of Canada, you mean it
21 is run as a separate government department?

22 COMMISSIONER LEMAN: Yes, it would be
23 removed from the control and influence of the Bank
24 of Canada.

25 COMMISSIONER MACKINTOSH: Presumably a
26 separate Crown corporation?

27 COMMISSIONER LEMAN: This has
28 been suggested to us as a desirable development, and
29 I just asked --

30 MR. MILNER: We have never frankly thought



1 of it, Mr. Leman. Just as a quick answer I could not
2 see where there would be any difference. Surely it
3 would be under the same aegis of government
4 control, and I would not think that it would change
5 the policy very much. I think what some people
6 have complained about was that the I.D.B. was infringing
7 on private enterprise in certain of their loaning
8 policies; that is, under the incorporation of the I.D.B.
9 it was supposed to be as I understand, a bank of
10 last resort where people who could not borrow elsewhere
11 were given government aid, and the difficulty with
12 I.D.B. as I see it -- the same difficulty, of course,
13 exists in the finance companies to some extent -- that
14 a lot of people that are borrowing from those two
15 sources, that what they really need is capital and
16 not borrowed money. It is not loans they want, it
17 is some capital, and I think that this new corporation
18 that has been formed generally by one of our members
19 here, plus a lot of the larger institutions, is along
20 the lines that we believe can be of great benefit to
21 the country for the period of years where they are
22 supplying capital, straight capital, to enterprises,
23 which is what the enterprises need, rather than borrowed
24 money, and if the bank were divorced from the Bank
25 of Canada, -- the I.D.B. -- I do not see that it would
26 necessarily change this policy.

27 COMMISSIONER LEMAN: These other people
28 must have thought it might because this is the suggestion
29 that they made.

30 At the end of both sections -- and I have



1 mentioned I and L -- you end up with a recommendation
2 in each case that some change be made in the tax
3 structure to provide an incentive for raising capital
4 investment, and more specifically in the small businesses.
5 Well, that is something one often resorts to, but do
6 you believe in general that we ought to start plugging
7 our tax structure? After all, there is a little
8 problem that crops up in the economy where they pay
9 some kind of a tax incentive.

10 MR. MILNER: No, I think that would be
11 the worst thing one could do.

12 MR. BEATTY: In this type of high risk
13 operation that is envisaged, the provision of a reserve
14 is the type of tax incentive that might make it worth-
15 while.

16 MR. SHAW: This is the sort of thing that
17 has been used in European economies to encourage new
18 risk capital; the sort of thing that has been done,
19 I believe, in West Germany where they exempt from
20 taxation, from your taxable income, the amount of money
21 that you put into a new venture. That is generally
22 the approach, without going into the details of the thing.
23 This is the incentive to the man with the capital to
24 put his money into a risk venture and he shares the
25 burden with the government, but it seems to work.

26 MR. MILNER: Could I ask Mr. Leman to
27 speak on that as well?

28 MR. LEMAN: I would like to say a few things
29 concerning the Industrial Development Bank. It has
30 been the feeling of this Association that the bank



1 should not operate in economic spheres where underwritings
2 by our Association are available at reasonable cost. In
3 practice this has been found to be in direct competition
4 with the Industrial Development Bank but only on rare
5 occasions do we recognize it..

6 The other aspect of the operation lies
7 in the most beneficial way in which it might operate
8 in favour of small businesses; we do not pretend that
9 this organization should be self liquidating, but we
10 feel it should be a non-profit making organization and
11 that if in support of sound management the security
12 required for each loan is high, it could all be
13 realized on repayment of the loan and not retained
14 to create reserves as security against future risks.
15 The feeling of the I.D.B. is that it is very onerous
16 on the small operator, and besides giving three or
17 four or five year term loans they want additional
18 security in the form of bonus shares or common shares
19 and to retain these shares once the loan has been re-
20 paid, which accounts substantially for the important
21 amount of surplus accumulated in the investment
22 development.

23 COMMISSIONER LEMAN: On that section, the
24 I.D.B. is run as a completely non-profit organization
25 but circumstances flow from that. First of
26 all, it would definitely be more competitive with the
27 private sector than if it operates at a profit?

28 MR. LEMAN: Well, the answer to that is
29 the fact that in principle, there are members who
30 welcome any and all enquiries for underwriting purposes.



1 There are no corporate ventures which are not included
2 in the services of our members. Some difficulties
3 arise in the size of the borrowings desired and the
4 quality of the management may be of the essence, but
5 in principle we welcome any and all borrowers who
6 request the services of our members.

7 COMMISSIONER LEMAN: I think this is all
8 I have.

9 COMMISSIONER MACKINTOSH: Could I go back
10 to your earlier answer, Mr. Leman. I understood
11 you to say in cases where the borrower had paid back
12 his loan that the I.D.B. ought to return the bonus
13 shares they had taken.

14 MR. LEMAN: Well, the I.D.B. does not
15 necessarily retain them, but they sell those shares
16 back to the owners of the business.

17 COMMISSIONER MACKINTOSH: Oh.

18 MR. LEMAN: And it turns out to be a
19 very onerous operation on the part of the borrower.

20 COMMISSIONER MACKINTOSH: Does he have
21 to buy them?

22 MR. LEMAN: Well, his capital structure
23 is left in the hands of the I.D.B.; it is a measure
24 of security. It is sound management from the point
25 of the I.D.B. to enable it to take over a venture
26 if it is not running properly, but if the operation
27 has been successful and the loan has been repaid, well
28 the I.D.B. could move out of the picture without
29 penalizing the owners of the business to that extent.

30 COMMISSIONER MACKINTOSH: What about the



1 incidenc : where they took bonus shares and the venture
2 did not succeed?

3 MR. LEMAN: Well, the I.D.B. loans only on --
4 they have the security there. Some of their loans
5 have turned sour, but the experiences ^{has} /shown that there
6 has been \$18 million surplus accumulated over the
7 period of years that the bank has been operating and
8 the outstanding loans totalled \$75 million at the end
9 of last year, which shows a pretty sound reserve for
10 future risks they might take.

11 COMMISSIONER LEMAN: I have one last
12 question in a completely different field. We have
13 heard a lot through the brief and through the dis-
14 cussion about call loans. Are such loans called?
15 Is there a record of their being called often?

16 MR. SHAW: We refer to them as "so-called
17 loans"!

18 COMMISSIONER LEMAN: They are not called?

19 MR. JOHNSON: There are occasions when they
20 are called, but very rarely.

21 MR. LEMAN: But very rarely.

22 COMMISSIONER LEMAN: Would there be a case
23 for a monetary policy if they should be called more
24 frequently in response to monetary conditions?

25 MR. SHAW: I find difficulty in seeing
26 the purpose of that other than to embarrass the members
27 of our industry who might be enjoying the loan. What
28 purpose would there be in recalling -- these are the
29 lateral loans which we use from day to day in our
30 business and apart from the ones that apply to many markets;



1 is it your suggestion that the monetary policy would
2 be to restrict the operations of the dealers by suggesting
3 to the banks that they reduce the amount of loans
4 outstanding to the dealers?

5 COMMISSIONER LEMAN: Is not the point that
6 you want to make here that you have to at certain times
7 finance with the country banks?

8 MR. SHAW: That is a matter of economics.

9 COMMISSIONER LEMAN: But presumably the
10 rates are different, are they not?

11 MR. SHAW: Quite substantially.

12 COMMISSIONER LEMAN: Therefore, would it
13 not be a further instrumentation of the monetary policy
14 if they were called in?

15 MR. SHAW: And force out into the country
16 banks the few that are left with the chartered banks?

17 COMMISSIONER LEMAN: Yes.

18 MR. SHAW: Or absolve it.

19 MR. ELY: You mean that the monetary policy
20 might use that device to shrink the overall loan
21 position by having the loan called and the security
22 that was lodged against that loan sold?

23 COMMISSIONER LEMAN: Perhaps in the same
24 way that happens to the bank.

25 MR. SHAW: I think that we would consider
26 that an undesirable development!

27 COMMISSIONER GIBSON: This is in connection
28 with the effect of interest rates and credit conditions
29 on the investment dealers; in other words, how does
30 the monetary policy work through the investment organization.



1 To be a little more specific, in tight money, in
2 1956 and 1957 and again in 1959, what happened to the
3 supply of funds for the new issues? Did they tend to
4 dry up?

5 MR. MILNER: The availability for new issues?

6 COMMISSIONER GIBSON: Yes, indeed.

7 MR. MILNER: Yes, during some of that period
8 there was definitely a rationing of issues. In other
9 words the interest rate took care -- not rationing,
10 but the interest rates ---

11 COMMISSIONER GIBSON: The interest rates did
12 the rationing?

13 MR. MILNER: That is right.

14 COMMISSIONER GIBSON: And this was effective;
15 in other words, it cut the demand down to fit the reduced
16 supply?

17 MR. MILNER: Yes; take, for instance, in the
18 municipal field: There was a number of instances in
19 the municipal field where the improvements a municipality
20 wanted to put in had to be postponed for a year on
21 account of the interest rate.

22 MR. SHAW: Specifically, I believe cases could
23 be found where pending underwritings at that time were
24 deferred because the underwriter involved did not have
25 the assurance that he needed that loan accommodation
26 would be available to him at his bank.

27 COMMISSIONER GIBSON: For him to underwrite
28 the loan?

29 MR. SHAW: If I understand your question correctly,
30 does this tight money condition -- under the loan ceiling



1 the only course left to the bank is that of rationing
2 the available resources they have, and in such a period
3 the underwriter would be very prudent if he were to
4 have discussions with his bank to find out if he
5 fitted into their rationing programme at the time.

6 COMMISSIONER GIBSON: In other words, credit
7 rationing by the bank meant less funds were available
8 through the new issue market?

9 MR. SHAW: It could have been. It didn't turn
10 out to be serious because in that particular period
11 the climate was not good for an underwriting, in any
12 event.

13 COMMISSIONER GIBSON: Well, how much did the
14 supply of new funds fall off in these two periods?
15 Was it a sharp reduction?

16 MR. SHAW: No.

17 MR. BEATTY: It was a sharp reduction in the
18 corporate field.

19 MR. SHAW: Not for the reason the underwriter
20 could not secure the accommodation, although it was
21 a factor in the odd case, but it was simply that the
22 whole investment climate was such that the underwriter
23 would not mount an issue until the conditions clarified.

24 COMMISSIONER GIBSON: Looking at it the other
25 way round, did the high interest rates cause many
26 postponements and deferments, and so on? Would you give
27 a few examples of this sort of thing?

28 MR. SHAW: We made some effort to find cases
29 where that happened and found some difficulty in finding
30 specific instances where a borrower was steered away



1 from the market because of the cost of his money.

2 It was more a concern about the success of his issue
3 almost under any reasonable interest rate terms.

4 COMMISSIONER MACKINTOSH: Of course, isn't
5 that the same thing? If the borrower says, "I would
6 be willing to pay more. I would be willing to pay
7 anything reasonable", but the underwriter says, "To
8 really make this issue a success you have got to pay
9 a little more than is reasonable"?

10 MR. SHAW: I think what would more likely
11 happen is that the underwriter would advise his client
12 against coming to the market under those conditions.
13 He would not wish to see the credit of that particular
14 corporation, which had enjoyed a relatively high rating,
15 being forced into another category, if you like, or
16 on to another shelf because of conditions which, according
17 to every expectation, would prove to be ---

18 COMMISSIONER MACKINTOSH: Whatever level you
19 take the decision off at, it is all the same compound
20 of reasons?

21 MR. MILNER: In other words, the effect was
22 decreased borrowing.

23 MR. SHAW: Deferment.

24 COMMISSIONER GIBSON: Where did you notice
25 this deferment most? You have been speaking of the
26 corporate field and the municipal field.

27 MR. SHAW : I would think it became most
28 apparent in the municipal field at that time with the
29 deferment on the part of individual municipalities
30 coming to the market under those conditions, deferring



1 their financing until a later date, but I would certainly
2 like to hear other expressions on that.

3 MR. BEATTY: I would agree. The lower quality
4 corporate borrower too deferred projects.

5 COMMISSIONER GIBSON: Did most of these
6 projects actually get deferred? In other words, did
7 people succeed in stirring up money from somewhere
8 else, to your knowledge, or were the projects actually
9 deferred?

10 MR. SHAW: There was a number of factors involved
11 including the effect on the judgment of the board of
12 directors of the company. In such times their attitude
13 towards expansion is certainly affected if the whole
14 situation is not particularly promising. The psychological
15 effect upon the people who are planning expansion
16 is particularly noticeable in such difficult times.

17 COMMISSIONER GIBSON: You think these tight
18 money periods have really caused quite a deferment
19 of expansion in the corporate as well as the municipal
20 field, do you?

21 MR. SHAW: I can't give you specific evidence
22 that that was so in so far as giving you illustrations
23 of cases where it happened, but I would express the
24 general view that in total there probably was a considerable
25 amount of deferment developed in 1959.

26 COMMISSIONER GIBSON: And 1956, 1957.

27 MR. SHAW: That period.

28 COMMISSIONER GIBSON: In the corporate fields
29 did you see much evidence of people going to other
30 sources, particularly to the United States, to get the



1 money?

2 MR. SHAW: No.

3 MR. ELY: Not necessarily, because most of
4 the Canadian corporations have earnings in Canadian
5 dollars and would be unwilling to commit themselves
6 to paying American funds for their money.

7 COMMISSIONER GIBSON: Some of them, of course,
8 have corporate relationships with the United States?

9 MR. ELY: Yes, they would sometimes look to
10 that market but only if they had an income in the
11 countries where they were borrowing other than Canada.

12 COMMISSIONER GIBSON: What about your portfolio
13 management advice during change of money conditions?
14 In tight money, for example, is the sort of advice
15 you give to your clients a very radical change to
16 reflect the monetary conditions?

17 MR. CRETZIANU: I would think that in periods
18 like today, when you can get very good returns on
19 short-term money, we would advise our clients to
20 keep their liquidities more in the short-term of the
21 market. Generally, you are penalizing a portfolio by
22 adopting a very liquid position. Either you keep the
23 cash, which gives you very little return, or short-term
24 securities which again gives you a low return when
25 compared to the long-term bonds. But at times such
26 as now, for instance, you can have the best of both
27 worlds and have both liquidity and a very good return.

28 COMMISSIONER GIBSON: And this, of course,
29 is a pretty marked change from the kind of advice
30 people would be given a year and a half ago?



1 MR. CRETZIANU: Certainly.

2 COMMISSIONER GIBSON: When money was easier
3 a year and a half ago, would there be a big switch
4 in advising people to go into stocks, and so on?

5 MR. CRETZIANU: It all depends on the nature
6 of the portfolio. We adopt for certain portfolios much
7 more defensive positions than for others. Take the
8 position, say, of an old person who has no other income
9 than his small pension and his portfolio: We would
10 advise a very defensive position, and whether money
11 was tight or easy we would certainly advise keeping at
12 least 30 or 40 per cent in long-term bonds in order to
13 have both a good return and a very defensive position.
14 On the other hand, a person with a good income of his
15 own, with adequate protection when he retires, certainly
16 would be advised to keep the bulk in equities in order
17 to try to build a capital position situation.

18 COMMISSIONER GIBSON: But is there quite a
19 change in the direction of investment -- let us say,
20 the change from 1956, 1957 when money was fairly tight
21 to 1958, 1959 or 1959, 1960 when it was fairly easy?

22 MR. CRETZIANU: As far as portfolio management
23 is concerned I still think it is at the short end
24 of the market that it would influence our decisions.
25 The factors which have brought tight money may induce
26 us to advise clients to switch their stocks because the
27 companies involved may be more vulnerable in periods
28 of stringent credit conditions.

29 COMMISSIONER GIBSON: Stringent credit conditions
30 are sometimes a reflection of the fear of inflation.



1 MR. CRETZIANU: Yes.

2 THE CHAIRMAN: There is just one question I
3 had in mind. Earlier in the proceedings there was
4 reference made to the activities of your members in
5 primary distribution of equities, and I gathered the
6 impression that you did quite an extensive business in
7 primary distribution of equities, or what might be
8 called risk capital. You have a few paragraphs on risk
9 capital in the brief, and I don't think we have anything
10 in the brief, and we haven't heard yet any indication
11 of the magnitude of this sort of activity or the nature
12 of it, and I think for the record it might be well
13 to have some information of that kind.

14 MR. ELY: The magnitude of equity financing
15 in Canada?

16 THE CHAIRMAN: Through members of your
17 organization.

18 MR. ELY: I think members of the Investment
19 Dealers' Association probably do a very large volume
20 of equity financing. When you think in terms of the
21 amount of money through equities that have been raised
22 for the chartered banks, the utility companies such
23 as Bell Telephone, the steel companies, the gas pipeline
24 companies, and the oil transportation companies, and
25 many, many others, I would think from our records it
26 is a very large volume.

27 THE CHAIRMAN: Would there be any advantage
28 of having some more particular information of the
29 issues of that kind that have been made over the last
30 few years?



1 MR. BEATTY: It would be in the Bank of Canada
2 statistical summaries.

3 THE CHAIRMAN: Well, if we could have a reference
4 to that, that perhaps would be good enough.

5 MR. ELY: I think there are references to that,
6 Mr. Porter. I think you will find the volume is very
7 large.

8 MR. SHAW: It has been on a descending scale
9 in the last 10 years.

10 THE CHAIRMAN: During our hearings throughout
11 the country it has been pointed out from time to time
12 there are certain difficulties in raising equity capital.
13 It always seemed to me there was a great deal of equity
14 capital raised in this country from year to year, but
15 I would like to have it on the record of this Commission.

16 MR. SHAW: Something that might be added to
17 the record, Mr. Chairman, is that under the conditions
18 that prevailed in the last two years through the energies
19 of our association there has been repatriated to Canada
20 very substantial amounts of Canadian stocks which were
21 previously held by what we refer to as the N.R.O.
22 investment companies -- Non-Resident Owned investment
23 companies -- which were put together in great size over
24 a four or five year period from about 1954 to 1957 or
25 1958, which in the past two years, for one reason or
26 another, have been divesting themselves of these shares
27 and they have been returned to Canada and placed in
28 the hands of Canadian investors very largely through
29 the activities of members of our association. I think
30 that is an accurate statement.



1 MR. ELY: I think that is quite correct.

2 There has been a tremendous amount of repatriation,
3 of foreigners selling our Canadian equities and their
4 being absorbed into Canadian hands -- a very large
5 volume -- for the last two years all running in
6 one direction: Foreigners selling and Canadians
7 absorbing.

8 COMMISSIONER MACKINTOSH: Could you give a
9 rough idea in the equity capital raised of what the
10 proportion was to subscription rights and what by direct
11 underwriting?

12 MR. SHAW: The great weight of new capital,
13 the significant new equity capital raised in Canada
14 in the past four or five years would be through rights
15 by reason of the fact this capital was raised by larger
16 and more significant corporations expanding their
17 equity base.

18 MR. BEATTY: This is primary stock equity
19 capital. Preferred, of course, have gone the other
20 way.

21 MR. MILNER: Would you care to have us submit
22 some figures to the Commission, Dr. Mackintosh, as
23 to the total amount involved?

24 COMMISSIONER MACKINTOSH: I don't know that
25 is necessary.

26 THE CHAIRMAN: Personally, I would like to
27 see figures on the whole situation, not only on the
28 breakdown as to the rights aspect of it, but generally
29 speaking. I think it would be useful to have that
30 on the record.



1 MR. SHAW: Might I suggest, Mr. Chairman,
2 through your secretariat; any figures that have been
3 suggested here that they have not already put together,
4 or do not have readily available, that we might assist
5 in the gathering of that, and we would more than
6 willing to co-operate.

7 THE CHAIRMAN: Well, you see what we have in
8 mind, and see to what extent new enterprises have
9 been financed and equity financing, and existing
10 enterprises have expanded: It will be very interesting
11 to have that information.

12 MR. MILNER: We will get the information for
13 you, Mr. Chairman.

14 THE CHAIRMAN: In due course.

15 MR. MILNER: Yes, in due course.

16 THE CHAIRMAN: Gentlemen, thank you very much
17 for the vast amount of information you have contributed
18 to us in the last two days. It has been a very useful
19 discussion from our point of view and I hope it has
20 been from yours, and we appreciate very much indeed
21 the tremendous amount of work and the tremendous amount
22 of thought which you have put into the very comprehensive
23 brief.

24 MR. MILNER: Could I express, Mr. Chairman,
25 on behalf of everyone here our appreciation of the very
26 wonderful treatment we had at the hearings. We have
27 enjoyed every minute of the discussions. I know I
28 am speaking for everyone here.

29 THE CHAIRMAN: I think that enjoyment is from
30 hindsight. We will now adjourn until 8.45 A.M. tomorrow.

--- Adjournment.

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Royal Commission on Banking and Finance

Investment Dealers' Association of Canada.

Hearings
held at
Ottawa

Vol.

Date.

22A

11 & 12 JULY, 1962



Official Reporters
J.J. Nethercut and R.J. Young
Toronto, Ont.



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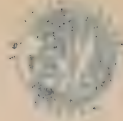


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FOREWORD

In planning the preparation of this Brief, The Investment Dealers' Association of Canada gave consideration to the size and scope of the subjects to be considered. The Association concluded that it would either have to obtain the services of professional consultants or that it would have to break up its presentation into a number of subjects and have one or more of its Members prepare memoranda on an assignment basis. It was appreciated that the latter method would produce considerable variety in style and approach, but these drawbacks were thought to be more than compensated for by the intimate knowledge on which our Members could draw in dealing with the subjects at hand. The memoranda supporting this Brief were, therefore, prepared on a "committee" basis.

The Association regrets that certain statistical and financial information which the Commission would like to have and, which it would like to offer, is not obtainable. Neither the individual firms nor the industry as a whole, have maintained records of the type which would enable detailed answers to some of the questions asked by the Commission on internal operations. In some cases, this information is not obtainable because of the overlapping nature of the stock, bond, money market and underwriting business. However, the trend toward centralized record-keeping, through the use of computers, may provide the inform-

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ation for more detailed analysis in the future.

A.J. Milner

President

The Investment Dealers' Association
of Canada.

June, 1962



RECOMMENDATIONS AND SUGGESTIONS

The following recommendations and suggestions are derived from and supported by the evidence and exhibits comprising Appendices A - N. These recommendations and suggestions appear in more detailed form at the end of the various appendices. A minority of members have indicated that they do not concur with those marked with an asterisk (*).

THE INVESTMENT DEALERS' ASSOCIATION OF CANADA RECOMMENDS

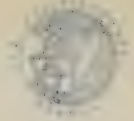
OR SUGGESTS:-

with respect to

I. GOVERNMENT OF CANADA ECONOMIC AND FISCAL POLICY:

REFERENCES

	<u>Appendix</u>	<u>Paragraph</u>
1. that a sound fiscal	B	22,32-40
policy be adopted immediately by the		
Government of Canada; that inherent	C	62,74
in this policy be the objective of		
approximately equivalating budgetary	Exhibit 44	
deficits which may be incurred in	F	32-39
recession years with surpluses in		
years of prosperity and that this policy		
be considered essential to the effective		
operation of the Bank of Canada and the		
maintenance and growth of a broad market		
for capital in Canada;		



RECOMMENDATIONS AND SUGGESTIONS

The following recommendations and suggestions are derived from and supported by the evidence and exhibits comprising Appendices A - N. These recommendations and suggestions appear in more detailed form at the end of the various appendices. A minority of members have indicated that they do not concur with those marked with an

Appendix (A)

OR SUGGESTS:-

with respect to

I. GOVERNMENT OF CANADA ECONOMIC AND FISCAL POLICY:

Appendix Paragraph

- I. That a sound fiscal policy be adopted immediately by the Government of Canada; that inherent in this policy be the objective of
- B 29, 32-40
- C 62, 74
- F 32-34
- deficits which may be incurred in recession years with surpluses in years of prosperity and that this policy be considered essential to the effective operation of the Bank of Canada and the maintenance and growth of a broad market for capital in Canada;



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2. that the Commission examine B 14-16
the areas of conflict between debt C 8 -13
management and control of currency Exhibits 5-7
with a view to determining whether
these functions should be separated;
3. that the Commission examine B 14-16
the Bank of Canada's role in operating F 50
the purchase fund and its trading for
Government accounts with a view to
determining whether these functions
should be handled by the Department
of Finance or other trading agencies;
4. that the Commission examine C 36,37
the Government's exchange policy with Exhibits 22-23
a view to determining the adequacy
of our exchange reserves, our position
vis-a-vis the International Monetary
Fund and the desirability of a
"pegged" rate;
5. that the Commission consider J 59
the valuable contribution of foreign
capital to Canada's post-war develop-
ment and recommend policies intended to
maintain a favourable investment climate
in Canada to ensure that this capital be
available, if and when needed;
6. that, to the extent that it is M 35-44
necessary or desirable to import capital Exhibit 2



Exhibits 22-23

Exhibits 22-23

that the Commission examine the areas of conflict between debt management and control of currency with a view to determining whether these functions should be separated; 3. that the Commission examine the Bank of Canada's role in operating the purchase fund and its trading for Government accounts with a view to determining whether these functions should be handled by the Department of Finance or other trading agencies; 4. that the Commission examine the Government's exchange policy with a view to determining the adequacy of our exchange reserves, our position vis-a-vis the International Monetary Fund and the desirability of a "pegged" rate; 5. that the Commission consider the valuable contribution of foreign capital to Canada's post-war development and recommend policies intended to maintain a favourable investment climate in Canada to ensure that this capital be that, to the extent that it is



REFERENCES

Appendix Paragraph

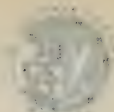
from foreign countries, Government of Canada policies be established which will encourage the purchase by foreigners of debt securities rather than equity investments of all kinds;

7. that the Commission examine G 57 the question of withholding tax on all foreign flows of short term investments into Canada's money market with a view to recommending that they be not discriminated against because they have little influence on the factors affecting non-resident control of Canadian resources and manufacturing;

8. that the federal budget address F 31 be delivered during the month of April each year;

9. that an informative public F 31 statement on the state of the nation be made by the Federal Government annually during the month of October;

10. that a standing committee B 61-65 composed of men from The Investment C 9-13 Dealers' Association of Canada having 21-28 35 experience and independent judgment Exhibit 7 13-19 in the marketing of Government of I 46 Canada Bonds be established by



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of Canada policies be established
which will encourage the purchase
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REFERENCES

Appendix Paragraph

Government decree to act in an
advisory capacity to the Bank of
Canada and the Department of Finance
in connection with such matters as the
marketing of Government of Canada issues
and open market and trading operations;

11. that an annual sinking fund of B 13
1 per cent of the principal amount of
Government of Canada issues with maturities
in excess of three years be established;

12. that the Commission examine the B 26-32
advisability of placing less emphasis on C 9(v)
Government financing through Canada
Savings Bonds and inquire into the proper
maximum limit of purchases of these Bonds
consistent with maintaining them as a true
savings instrument;

13. that the Government at the time B 63-64
of issue offer at least a substantial C 10
portion of all new issues to the public F 48
through normal channels at advertised
prices;

* 14. that the financing of the Canadian
National Railways and other Government B 66
agencies be arranged through large C 13
national syndicates composed of invest- Exhibit 7
ment dealers;

15. that, with the exception of 13 B 42-59



Government decree to act in an
advisory capacity to the Bank of
Canada and the Department of Finance
in connection with such matters as the
marketing of Government of Canada issues
and open market and trading operations;
11. that an annual sinking fund of B 15
1 per cent of the principal amount of
Government of Canada issues with maturities
in excess of three years be established;
12. that the Commission examine the B 25-32
feasibility of placing less emphasis on C
Savings Bonds and induce into the proper
maximum limit of purchases of these Bonds
consistent with maintaining them as a true
savings instrument;
13. that the Government at the time B
of issue offer at least a substantial C
portion of all new issues to the public F
through normal channels at advertised
prices;
14. that the financing of the Canadian
National Railways and other Government B
national syndicates composed of invest-



REFERENCES

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and 14 above, the present economic 67-76
and efficient methods employed in Canada
for treasury bill financing, marketing
of Government of Canada and provincial
issues be continued;
with respect to

II TAXATION:

16. that a Select Committee be N 35(2)(i)
formed to study and assess the entire (ii) / (iii)
tax structure of Canada with the objective
of devising an improved taxation system
better able to meet Canada's economic
needs; that before holding public
hearings such Select Committee carry
out its initial deliberations on a
confidential basis at the highest level
in order to arrive at some definite con-
clusions under objective conditions; that
such Sselect Committee be composed of highly
qualified individuals having a broad working
knowledge of the present tax structure with
most emphasis being placed on its practical
operation in ~~bus~~ business and in the economy
as opposed to its legal and accounting
operation and that such a Committee be
composed primarily of representatives of
business from members of The Canadian
Chamber of Commerce and Board of Trade,

67-76

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and efficient methods employed in Canada
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of Government of Canada and provincial
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with respect to

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composed primarily of representatives of
business from members of The Canadian



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Appendix Paragraph

representatives of finance from
members of The Investment Dealers'
Association of Canada and The Canadian
Bankers' Association, practical economists,
representatives of the Canadian Tax
Foundation, and, secondarily of members
of the legal and accounting professions;

17. that the Commission consider N 14-33
recommending that the twelve specific
areas of our tax structure outlined
in Appendix N be carefully studied, with
particular reference to:

(a) an incentive method of applying N 23
taxation;

(b) the use of indirect taxation as F 38 (2)
an alternative or partial N 19-22
alternative to personal and
corporation income tax;

(c) the tax disadvantage to Canadians, J 66
compared to U.S. citizens and N 31
corporations, in respect to
the development of Canadian oil
and gas natural resources;

(d) the merits of the 20 per cent tax I 17
credit and to the further reduction J 22-25
of double taxation in Canada N 26, 27

(e) the requirement of the Canadian N 29
economy for continuing and



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(b) the use of indirect taxation as F
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alternative to personal and
corporation income tax;
(c) the tax disadvantage to Canadians, I
compared to U.S. citizens and N
the development of Canadian oil
and gas natural resources;
(d) the merits of the 20 per cent tax I
credit and to the further reduction
of double taxation in Canada
(e) the requirement of the Canadian N



REFERENCES

Appendix Paragraph

substantial growth in which
an ever increasing quantity of
equity capital is essential and
which indicates that any capital
gains tax would be inadvisable and
not in the best interests of Canada;
and

(f) the merits of enabling a taxpayer
to obtain a tax ruling prior to N 30
a transaction;

18. that corporate income tax
legislation be amended to permit companies
to deduct financing costs as expenses; E 50
with respect to

III. BANK OF CANADA:

19. that the Bank of Canada Act be C 7
amended generally to clarify the Bank's Exhibit 4
relationship with the Government and
particularly to establish an improved
procedure for the resignation of the
Governor of the Bank of Canada either
by his own volition or by request of
the Government or parliament;

20. that the Commission examine C 44-60
the use of "moral suasion" by the Exhibits 31-42
Bank of Canada to influence such
things as stock margins, instalment



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 an ever increasing quantity of
 equity capital is essential and
 which indicates that any capital
 gains tax would be inadvisable and
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 and

(f) the merits of enabling a taxpayer
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 the Government or Parliament;

the use of "moral suasion" by the
 Bank of Canada to influence such



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Appendix Paragraph

sales, term lending by

chartered banks and the reserves

of "near banks";

21. that the Board of Directors C 18,19

of Bank of Canada be selected from Exhibit 12

men experienced in matters of

finance and business;

22. that direct participation C 19

of the Board of Directors of the Bank

of Canada in policy making be establish-

ed by having the executive committee

of the Board meet fortnightly and

the Board as a whole meet monthly;

23. that, in order to convey to C 41-42

the nation the economic health of the Exhibits 29-30

country, an administered bank rate F 40

be re-established;

x 24. that, in order to continue B 19-21

to foster the growth of the money G 45-48

market, the right of participants

to sale and repurchase agreements

with the Bank of Canada to the extent

of their lines of credit and at the

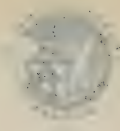
average weekly tender for 90 day

bills plus $\frac{1}{4}$ of 1 per cent be

continued; (for minority view see

Appendix C-43)

25. that closer liaison be G 48



continued: (for minority view see

dolls plus $\frac{1}{4}$ of 1 per cent be

average weekly tender for 90 day

of their lines of credit and at the

with the Bank of Canada to the extent

to sale and repurchase agreements

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Exhibits 29-30

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men experienced in matters of

of Bank of Canada be selected from

21. that the Board of Directors

of "near banks";

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REFERENCES

Appendix Paragraph

established between the Bank of
Canada and the money-market dealers
for the purpose of trading in money-
market securities;

*26. that the Commission consider C 40,60
recommending that the agreement between Exhibits 26,27
the chartered banks and the Bank of
Canada in 1956 establishing secondary
reserves be terminated;

27. that the Bank of Canada be C 17
urged to publish from time to time Exhibit 11
pamphlets intended to clarify the F 53
Bank's functions and actions;

* 28. that the trading departments C 29-30
of the Bank of Canada in Toronto and Exhibit 20
Montreal be given more authority;

29. that the Bank of Canada be F 46
urged to institute a programme designed
to expedite its replies to firm bids
or requests for firm offerings from
dealers;

with respect to

IV. SECURITIES REGULATIONS:

30. that S.E.C.-type legislation E 51-54
be not established in Canada and that
the Commission take note of the progress
already achieved towards uniform securities
legislation uniformly administered and



established between the Bank of
Canada and the money-market dealers
for the purpose of trading in money-

that the Commission considers
recommending that the agreement between
Exhibit 20

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Canada in 1955 establishing secondary
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that the Bank of Canada be
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Exhibit 11
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Bank's functions and actions;

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on requests for firm offerings from

with respect to

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be not established in Canada and that
the Commission take note of the progress
already achieved towards uniform securities



REFERENCES

Appendix Paragraph

the work presently in progress

to achieve this objective;

31. that the Commission examine K. 112-117

the protection provided under the 123

securities acts for shareholders of

both open and closed end investment

trusts and mutual funds and make

recommendations for such additional

regulatory legislation as may be

deemed advisable;

32. that the various securities E 55

acts be amended to permit the distribution

of preliminary prospectuses to prospective

securities purchasers;

with respect to:

V. JUNIOR GOVERNMENTS:

33. that the Commission consider B 33-40

recommending the use of savings loan

type issues by provincial governments

be sharply curtailed;

34. that life insurance companies D 22

be permitted to evaluate holdings of

municipal securities at the amortized

book value in the same manner as for

federal and provincial securities;

35. that school debentures, owned D 23

by non-resident insurance companies, be

accepted for deposit by the Federal



the work presently in progress

to achieve this objective;

the Commission

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securities acts for shareholders of

both open and closed end investment

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of preliminary prospectuses to prospective

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with respect to:

V. JUNIOR GOVERNMENTS:

33. that the Commission consider B

recommending the use of savings loan

type issues by provincial governments

whenever curtailed;

34. that life insurance companies D

be permitted to evaluate holdings of

municipal securities at the amortized

book value in the same manner as for

federal and provincial securities;

35. that school debtors, owned D

by non-resident insurance companies, be

excluded from the Federal



REFERENCES

Appendix Paragraph

Department of Insurance;

36. that no change be considered D 24
with respect to the tax status of Exhibit E
interest payments on municipal
debentures.

with respect to

VI. CHARTERED BANKS:

37. that every encouragement be given
to the continued healthy development of
the investment dealer's ability to
perform satisfactorily the important
underwriting function, and, in particular,

(a) that the banks continue
to refrain from making term loans in H 28
excess of a reasonable limit in amount 41-42
to business corporations where the time
of repayment is deferred beyond that of
ordinary bank loans and from purchasing
a security negotiated directly with the
customer as distinct from buying a
publicly issued security in the market
and

(b) that there be no further H 44-49
extension beyond the relatively few
cases of long standing which may exist,
of the inclusion of banks in syndicates
underwriting corporate securities for
resale to the public, particularly where



Department of Insurance;

36. that no change be considered in

with respect to the tax status of

interest payments on municipal

with respect to

VI. CHARTERED BANKS:

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customer as distinct from buying a

publicly issued security in the market

and

(b) that there be no further

extension beyond the relatively few

cases of long standing which may exist,

of the inclusion of banks in syndicates

underwriting corporate securities for



Appendix Paragraph

such inclusion would place the bank in the dual position of banker and underwriter and where the sale of corporate securities is for the purpose of paying off bank loans;

38. that section 91 of the Bank Act and section 71 (1) of the Quebec Savings Bank Act, which sections impose a ceiling of 6 per cent on rates that may be charged on bank loans, be repealed;

H 14-17

39. that the chartered banks be encouraged to adopt policies and procedures resulting in their call loan interest rate schedules being subject to periodic review and to take appropriate action to keep these rates in line with market conditions and competitive rates from other sources; with respect to

H 3-13

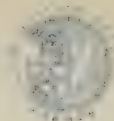
VII. FINANCING SMALL BUSINESS:

40. that the Commission consider recommending that special tax advantages be given to investment companies specializing in financing small businesses;

L 13

41. that the Commission consider recommending that the proceeds from loans to small businesses by institutional

L 2, 5, 9
10



such inclusion would place the

bank in the dual position of banker

and underwriter and where the sale

of corporate securities is for the

purpose of paying off bank loans;

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VII. FINANCING SMALL BUSINESS:

be given to investment companies

specializing in financing small

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41. that the Commission consider 2, 5, 2 I

recommending that the proceeds from



REFERENCES

Appendix Paragraph

investors be subjected to a
reduced corporate tax burden in
order to encourage this type of
financial activity;

42. that the banks and insurance L 3,5,8,9
companies be encouraged to apply a
portion of their funds to the
financing of small businesses through
equity purchases or long-term loans
to small business investment companies
similar to those operating under the
Small Business Administration Act
of the United States;
with respect to

VIII. MISCELLANEOUS

43. that the difficulty of obtaining
accurate statistics for assessing the G 16,24
roles of the various borrowers in the 29,36
money market be recognized and that 49
more information be obtained and published
concerning the borrowing by provinces,
municipalities and corporations in the
money market;

44. that the inadequacy of the J 20,27
statistical material available con- 31
cerning stocks and stock ownership
be recognized and that the Dominion
Bureau of Statistics assemble and



Appendix Paragraph

investors be subjected to a reduced corporate tax burden in order to encourage this type of

42. that the banks and insurance companies be encouraged to apply a

portion of their funds to the financing of small businesses through equity purchases or long-term loans to small business investment companies similar to those operating under the

of the United States; with respect to

43. that the difficulty of obtaining

accurate statistics for assessing the roles of the various borrowers in the money market be recognized and that

more information be obtained and published concerning the borrowing by provinces, municipalities and corporations in the

44. that the inadequacy of the

statistical material available concerning stocks and stock ownership be recognized and that the Dominion



REFERENCES

Appendix Paragraph

publish this material;

45. ~~United~~ that the Commission examine J 65
the participation in the stock Table 15
market of Canadian financial
institutions and pension funds
in comparison with those in the
U.S. and make such recommendations
as will encourage increased
participation by them;

46. that the Commission examine E 57
the important matter of expropriation
of electric utilities with a view to
recommending that the Federal Government
devise means to minimize the temptation
to expropriate arising out of Federal
tax treatment of the provinces;

47. that the Commission examine E 58
shareholders rights in the light of
certain recently employed "take-over"
techniques;

48. that the Commission examine E 59
the Companies Act of Canada with a
view to recommending removal of certain
anomalies in it which tend to deter the
incorporation of companies under its
provisions.

That in its deliberations on this



1947

1947

46. that the Commission examine

Table 15

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U.S. and make such recommendations

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anomalies in it which tend to deter the

incorporation of companies under its

provisions.



Nethercut & Young

Toronto, Ontario

A.18

1 and other submissions the Commission be
2 aware that the Investment Dealers' Association
3 of Canada believe it to be in the best interest
4 of Canada, that, insofar as is possible the
5 changes which the Commission deems it advisable
6 to recommend be induced by the provision of suitable
7 incentives rather than through legislative action.



S U M M A R Y

(The following is a summary of Appendices A to N which contain the detailed evidence supporting this Brief).

THE INDUSTRY AND THE ASSOCIATION

The Industry - Appendix A (part 1)

1. The investment business as we know it today dates back to the 1880's. At the outbreak of the 1st World War, over three-quarters of all new issues of Canadian bonds were still being placed in London. It soon became necessary for Canada to turn to domestic sources to finance the war effort. In six loans the investment community was able to raise over \$2.2 billion from 2.8 million subscribers. The magnitude and success of this effort stimulated the rapid development of the industry in Canada.

2. In 1920 a committee of dealers and banks was formed at the request of the Minister of Finance to deal with a heavy return flow of securities from London. Redistribution of \$150 million of Victory Bonds was achieved and an orderly market maintained. During the 1920's over 80 new investment firms were formed. In this period the upsurge of industrial development induced a large volume of corporate financing. The size of new issues increased and the industry rapidly developed the methods of underwriting corporate and government securities, which, while modified and improved, are still in existence today.

3. Subsequent to 1929 the industry underwent a period of trial as earnings, tax collections and

S U M M A R Y

(The following is a summary of
Appendices A to N which contain
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THE INDUSTRY AND THE ASSOCIATION

The Industry - Appendix A (part 1)

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3. Subsequent to 1929 the industry underwent



1 security prices declined precipitously. The
2 disruption of markets which occurred when Britain
3 went off the gold standard caused a serious crisis
4 and impressed dealers with the need of speeding up
5 the distribution of new issues. In general, the
6 decline in volume of new issues in the 30's led to a
7 greater emphasis on secondary market trading, a
8 concentration on security analysis and an increasingly
9 sophisticated approach to financial matters resulting
10 in part from detailed work done on corporate re-
11 organization and debt re-adjustment.

12 4. During the 2nd World War the securities
13 business was centred in the work of the National
14 War Finance Committee. In the war period over 23
15 million subscriptions were obtained for the various
16 loans which totalled \$13.1 billion.

17 5. As the post-war period began, the industry
18 was convinced by its wartime experience that there
19 could be a large increase in the securities business.
20 Low interest rates, inflation, the liquidity of
21 investors based on government bondholdings and the
22 favourable economic environment encouraged a strong
23 trend toward equity investment. Increased financial
24 capacity and the employment of more highly trained
25 staff enabled dealer organizations to underwrite
26 and distribute larger issues and generally to expand
27 their business.

28 6. The post-war period saw the Bank of Canada
29 become the dominant factor in the high-grade bond
30 market. Since the Bank introduced the money market



425

security prices declined precipitously. The disruption of markets which occurred when Britain went off the gold standard caused a serious crisis and impressed dealers with the need of speeding up the distribution of new issues. In general, the decline in volume of new issues in the 30's led to a greater emphasis on secondary market trading, a concentration on security analysis and an increasingly sophisticated approach to financial matters resulting in part from detailed work done on corporate re-organization and debt re-adjustment.

4. During the 2nd World War the securities business was centred in the work of the National War Finance Committee. In the war period over 25 million subscriptions were obtained for the various

5. As the post-war period began, the industry was convinced by its wartime experience that there could be a large increase in the securities business. Low interest rates, inflation, the liquidity of investors based on government bondholdings and the favourable economic environment encouraged a strong trend toward equity investment. Increased financial capacity and the employment of more highly trained staff enabled dealer organizations to underwrite and distribute larger issues and generally to expand.

6. The post-war period saw the Bank of Canada become the dominant factor in the high-grade bond



1 in June 1954, investment dealers have generated a large
2 volume of trading in short-term securities. The 1950's
3 saw a great expansion in the sale of Canadian securities
4 to foreigners. The post-war period illustrated again
5 the ability of the industry to adjust to changing
6 conditions, demands for funds and investor preferences.
7 As at December 31st, 1961, The Investment
8 Dealers' Association of Canada (I.D.A.C.) had 189 Members
9 directly employing 9,329 people, of whom 14.5 per cent
10 were partners and directors. A survey in August 1958
11 showed the industry employing 8,589 people in 196 firms.
12 Thus, in this period, while membership declined by 7
13 firms, the number of personnel increased some 8 per
14 cent. These figures indicate a trend in the industry
15 toward rising employment based on the need for a larger
16 number of office workers, analysts, traders and the
17 like to support each salesman. 110 I.D.A.C. members
18 have staffs of 25 or less and of these some 60 employ
19 less than 10 persons. In the main these small firms
20 have been built on the knowledge, capital and sales
21 ability of a few senior partners.

22 8. Appendix A (part 1) describes the internal
23 organization of an investment house. One important
24 common denominator of all firms except those few which
25 are controlled in the United States, is that without
26 exception the officers, partners, and directors
27 actively participate in the business.

28 9. The investment business in Canada is
29 characterized by the great variety in the size, type
30 of business, and the kind of clientele of the various



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Dealers' Association of Canada (D.A.C.) had 189 members directly employing 9,329 people, of whom 14.5 per cent were partners and directors. A survey in August 1953 showed the industry employing 8,589 people in 196 firms. Thus, in this period, while membership declined by 7 firms, the number of personnel increased some 8 per cent. These figures indicate a trend in the industry toward rising employment based on the need for a larger number of office workers, analysts, traders and the like.

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9. The investment business in Canada is characterized by the great variety in the size, type



1 firms. Broadly speaking, the integrated houses are
2 the large national firms which underwrite, distribute,
3 trade, and evaluate practically all types of securities.
4 Distributing houses do not customarily originate
5 industrial issues but participate in their distribution
6 and carry on trading in outstanding securities.

7 Specialty houses are those which restrict their business
8 primarily to such areas as unlisted stock trading or
9 buying and dealing in municipal or religious issues.

10 '10. Underwriting is a principal function of the
11 investment dealer. The dealer underwrites by buying
12 all or part of an issue for his own account or jointly
13 with others, by winning a public tender for securities
14 and by negotiating new issues. While not underwriting
15 in a strict sense other methods of acquiring new issues
16 used by underwriting houses include arranging private
17 placements and acting as agent for issuers. Under-
18 writing firms form a key group in the list of primary
19 distributors which the Bank of Canada uses for offering
20 new Government of Canada issues. In provincial issues
21 large national underwriting syndicates may negotiate
22 for the purchase of the issue or in the case of smaller
23 issues several such syndicates may bid at public tender.
24 Municipal issues are bought by underwriters through
25 public tender or purchases arranged by private
26 negotiation. Government of Canada money market issues
27 are dealt in primarily by 14 investment dealers and the
28 chartered banks. The Treasury Bill segment of this
29 market represents a large volume of transactions at
30 very small margins. Bills are tendered for each week



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1 at public auction. Corporation issues are generally
2 underwritten after direct and private negotiations between
3 an underwriting house and the company. In these issues
4 the investment dealer assists in designing the issue
5 in accordance with the requirements of the company and
6 the current preferences of the market. The underwriting
7 function as applied to the various types of securities
8 outlined above, is described in detail in Appendix A
9 (part 1).

10 11. Another major function of the investment
11 dealer is that of trading in outstanding securities.
12 Through his trading activities the dealer establishes
13 and maintains markets and thus provides liquidity and
14 establishes value levels for securities not listed
15 on exchanges. Most dealers active in secondary markets
16 carry inventories which enable them to conduct an
17 orderly market and to deal in the size required by
18 financial institutions. The street market of the dealers
19 is handled by their traders. The larger firms will have
20 a number of traders who may specialize in money market
21 securities, Canadas, provincials, corporates and
22 unlisted stocks. This trading is done through a network
23 of direct telephones and other communications facilities
24 on a truly national basis. The kingpin of this market
25 is the Bank of Canada whose prices and actions with
26 respect to money market securities and Government of
27 Canada bonds provide the bench for the "government" market
28 and for the evaluation of lesser securities. While
29 market information is passed on by word of mouth,
30 printed information, primarily quotations is disseminated

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1 regularly by some 25 dealers and the I.D.A.C.

2 12. A third and increasingly important function
3 of the investment dealer is the provision of a variety
4 of services. Advice to buyers, sellers, and issuers
5 of securities is given through interviews, telephone
6 communications, memoranda, analytical reports and the
7 like. In addition, the dealer's growing business and
8 the increasing sophistication of his clients is requiring
9 provision of more information in the form of economic
10 and industry studies, market commentaries, offering
11 lists, notification of called bonds, etc. Portfolio
12 management services are offered to clients by a number
13 of dealers. The rapid growth in the demand for these
14 services in recent years has necessitated that dealers
15 expand their research and clerical staffs.

16 13. In contrast with other financial institutions,
17 investment dealer organizations are small and character-
18 ized by a high degree of independence and individuality.
19 Over the years they have adapted themselves to changing
20 conditions in a manner which has resulted in a continual
21 broadening of the Canadian capital market. Mr. J.E.
22 Coyne, then Governor of the Bank of Canada, in a
23 public address made on December 14, 1959, stated:

24 ".... we also have in Canada a well
25 developed nation-wide capital market,
26 particularly in respect of the distribution
27 of securities issued by governments, local
28 authorities and business corporations. This
29 is primarily the field of activity of
30 investment dealers. I think there is little

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doubt that the financial machinery existing in Canada for the placing of new issues of securities on the market is the equal of that of any country in the world and, in proportion to our size, it probably arranges, year in and year out, for the provision of a greater quantity of new capital to those requiring it than is the case in any other country in the world. The results achieved are a reflection of the industry and enterprise and broad national outlook of our investment dealers...."

The Association - Appendix A (part 2)

14. The Association (The Investment Dealers' Association of Canada) was formed in June 1916 under the name of the Bond Dealers' Association of Canada with 32 members. By 1920, membership had grown to 104 and in 1939 there were 130 members. Peak membership of 206 was reached in 1958 and since this time membership has declined to 189. In 1925 the name was changed to the Investment Bankers' Association of Canada but with the passage of the Bank Act in 1934 use of the word "bank" was restricted and the name of the Association had to be changed to The Investment Dealers' Association of Canada (I.D.A.C.)

15. Membership in the Association is governed by its constitution and by-laws. Membership is open to all those carrying on business as investment dealers if it can be shown that at least one-half of their gross



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changed to the Investment Dealers Association of
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of 206 was reached in 1998 and since this time membe-
104 and in 1999 there were 180 members. Peak membership
with 52 members. By 1990, membership had grown to
the name of the Bond Dealers Association of Canada
Association of Canada) was formed in June 1973 under
The Association - Appendix A (Page 2)



1 profits result from underwriting, distributing or
2 buying and selling investment securities in Canada. It
3 is required that at least 50 per cent of the partners
4 or officers and directors must have been in the invest-
5 ment business for at least five years. Minimum standards
6 varying with the type and size of the business are set
7 to prescribe the amount of capital each member must
8 maintain. The by-laws of the Association have been
9 continually amended to reflect the changing standards
10 and requirements of the industry.

11 16. The I.D.A.C. is organized on a national
12 basis and for its purposes Canada is divided into six
13 districts with the chairman of each district executive
14 committee being a vice-president of the Association.
15 Each district has a Business Conduct Committee, and
16 there is a National Business Conduct Committee. The
17 National Association has a permanent executive staff
18 at its head office in Toronto and at its branch office
19 in Montreal. The I.D.A.C. is not directly comparable
20 with associations in other countries.

21 17. A principal function of the I.D.A.C. is the
22 protection of the investing public by endeavouring to
23 maintain the highest standards of ethics and reliability.
24 As a control the I.D.A.C. makes all members subject to
25 periodic routine reviews of the type of business they
26 conduct. The I.D.A.C. also devotes considerable time
27 to the protection of its members and to the advancement
28 of Association objectives by taking a broad interest
29 in economic, legislative, tax and other matters. This
30 brief is an illustration of that interest. While day-to-



1 day control over securities trading is carried on by the
2 Bond Traders' Association of Toronto and Montreal, the
3 I.D.A.C. exercises ultimate responsibility for regulating
4 secondary trading.

5 18. Another prime function of the I.D.A.C. has
6 been to provide education on investment matters for
7 employees of its members and for the general public.
8 Since the inception of the employee education programme
9 in 1947, 5,996 persons have enrolled in the two courses
10 provided and 3,601 have successfully completed at least
11 one of these courses. A third course is now being
12 prepared which is designed to improve employees'
13 knowledge of the banking, accounting, contractual,
14 regulatory and legal aspects of the investment business.
15 Each year the I.D.A.C. has distributed through several
16 universities a home study correspondence course
17 entitled "How to Invest Your Money in Bonds and Stocks".
18 A total of 20,000 persons have enrolled in these
19 courses. Also in co-operation with universities and
20 school boards, the I.D.A.C. has established lecture
21 courses in which 1,700 Canadians were enrolled in 1961.
22 By using voluntary speakers panels composed of members,
23 the I.D.A.C. now provides about 100 public addresses
24 a year for various organizations. Its film "A Matter
25 of Importance" has received over 300 showings since it
26 was produced in 1954. Through these and other means,
27 the I.D.A.C. is making a serious effort to improve
28 the public's knowledge and understanding of investments
29 and the investment business.

30 19. Apart from occasional surveys, the I.D.A.C.



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Each year the I.D.A.C. has distributed through several
universities a home study correspondence course
entitled "Investment in Canada". This course is
designed to provide a general knowledge of the
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1 has not been a statistics gathering body. The year-ends
2 of its members are scattered throughout the calendar
3 year and no two firms keep their books in the same way.
4 It may be desirable in the future to standardize account-
5 ing practices to a greater degree. This would make the
6 regular collection of statistics feasible. The I.D.A.C.
7 does make a contribution by gathering and assembling
8 figures on member borrowings outside of the banks, and,
9 in co-operation with D.B.S., by assembling and distribut-
10 ing information on the sales and purchases of securities
11 between Canada and other countries. Each business day
12 the I.D.A.C. makes available quotations on a large
13 and representative list of bonds and debentures traded
14 in Canada. The I.D.A.C. has prepared and produced a
15 number of publications which have been found to be
16 valuable within and without the industry. Copies of
17 these are exhibited.

18 20. In addition to these specific functions,
19 the I.D.A.C. has made important contributions by
20 virtue of its liaison activities with many bodies such
21 as the Canadian stock exchanges and the Canadian Bankers'
22 Association.

23
24 FINANCE DEPARTMENT & FEDERAL & PROVINCIAL FINANCE

25 - Appendix B

26 21. The Second World War brought about such great
27 changes in the Canadian debt structure and in debt
28 management that study of pre-war conditions would have
29 no real significance. Also, the inflationary forces
30 created during the war, together with the deferred



FINANCE DEPARTMENT & FEDERAL & PROVINCIAL FINANCE

- Appendix B

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1 demands for all forms of social capital, both from
2 within Canada and from foreign countries, greatly
3 stimulated capital expenditure. Low interest rates
4 and rapid economic expansion induced a vastly increased
5 volume of Canadian and foreign investment into the equity
6 field. The public tended to reduce the proportion of
7 federal government bonds in their portfolios and there
8 was a growing reluctance on the part of many investors
9 to apply more than a limited portion of their funds
10 to long-term bonds. While certain important institution-
11 al groups are obliged to buy fixed income securities,
12 even these tended to apply higher proportions to better
13 yielding securities and equities. These developments
14 have tended to narrow the market for long-term Federal
15 Government bonds.

16 22. In the latter part of the 1950's, the
17 government accepted the principle of deficit financing
18 as a stimulus to a lagging national economy. Lack
19 of investor interest in long-term debt securities
20 necessitated the government financing its requirements
21 largely in the short-term market and through Canada
22 Savings Bonds, which latter, now comprise 22 per cent
23 of the government debt. These activities have tended
24 to distort the bond market and reduce the liquidity
25 of long-term Bonds. The increasing dependence on
26 financing through Canada Savings Bonds, which are in
27 effect demand obligations, rather than through term
28 issues, is a regrettable trend.

29 23. The root of the problem is fiscal policy.
30 It would probably have been impossible to finance the



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financing through Canada Savings Bonds, which are in
effect demand obligations, rather than through term
issues, is a regrettable trend.



1 large deficits of recent years by other means. Fiscal
2 policy should direct more attention to debt retirement
3 in periods of prosperity. This, combined with provision
4 of a fixed annual sinking fund of 1 per cent per annum
5 on all outstanding federal government issues over
6 three years, would provide the market with the confidence
7 it needs.

8 24. It appears that there is a tendency for debt
9 management policy to be unduly subordinated to monetary
10 policy and it is suggested that the Royal Commission
11 inquire as to whether debt management and control of
12 currency have conflicting interests and whether these
13 functions should be separated.

14 25. It seems appropriate to study the possibilities
15 of returning to an administered Bank Rate, which would
16 clearly indicate the state of the Canadian economy.
17 In order to foster the growth of the money market,
18 the money market participants should continue to have
19 the right to sale and repurchase agreements with the
20 Bank of Canada, at the average weekly rate established
21 at the tender for 90-day Bills, plus $\frac{1}{4}$ of 1 per cent.

22 26. In the last five years large federal
23 government deficits have necessitated substantial
24 increases in debt. Now, out of a total debt of \$18.6
25 billion, only \$8.4 billion or 45 per cent is for a fixed
26 period of over 3 years. Nearly \$4.1 billion or 22 per
27 cent consists of Canada Savings Bonds. Savings Bonds
28 are designed for individual investors of modest means.
29 They encourage the ownership of liquid assets by a
30 large number of families who might not otherwise be



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1 inclined to save. Thus they play an important part in
2 Canada's financing. However, in view of the large
3 amount now outstanding and the high cost of this type
4 of financing, we suggest that the Government should place
5 less emphasis on financing through this type of medium
6 and that the maximum to any one buyer be limited,
7 consistent with maintaining a true savings instrument.
8 27. In Appendix B, a comparison is made between
9 methods of financing short and long term government
10 and provincial securities in Canada with the methods
11 used in Great Britain and the United States. The
12 Canadian methods appear to be well suited to the
13 requirements of this market. Indeed, they represent a
14 combination of adoption and evolution starting during
15 the First World War and the result seems particularly
16 appropriate for our requirements. The syndicate method
17 of negotiating for, or bidding on, provincial issues
18 has evolved into a very satisfactory method of purchase
19 and distribution. However, ways and means could be
20 found to improve the liaison between the investment
21 community, the Finance Department and the Bank of Canada
22 which could probably result in more efficient and
23 effective marketing of new Government of Canada issues.
24 To achieve this objective, a standing committee on the
25 marketing of government bonds should be established by
26 Government decree.

27 28. Because of the Federal Government's control
28 of the money supply, the dangers of it relying on
29 short issues and Savings Bonds are not as great as is
30 the case with the Provinces. In the main, it would seem



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1 that the Provinces should issue short term securities
2 or savings-type securities only under conditions when
3 long term credit is not readily available. Provincial
4 borrowing is primarily for long term projects and long
5 term debt should be issued against these projects.
6 The large requirements of the provinces can only be
7 raised by strong groups of dealers. In the case of the
8 larger provinces national syndicates are needed to
9 handle their requirements.

10
11 BANK OF CANADA - Appendix C

12 29. The recommendation of the Royal Commission
13 on Banking and Currency in Canada under the Chairmanship
14 of Lord MacMillan prepared the way for the establishment
15 of the Bank of Canada and the delineation of most of
16 its functions. It soon became evident that while the
17 Bank should have freedom in implementing monetary policy,
18 such policy must be in agreement with that of the
19 Government. The unhappy events of 1961 suggest the
20 need of a formal procedure to solve disagreements
21 between the Government and the Bank on both fiscal and
22 monetary policy.

23 30. The original Bank of Canada Act (1934)
24 provided that the Bank was responsible for debt
25 management, but it did not actually become the
26 Government's agent until 1938. Since this time and
27 particularly with the growth of the welfare state
28 concept, debt management has tended to cause a conflict
29 of interest for the Bank. The Bank's objectives are
30 "to regulate credit and currency in the best interests



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1 of the economic life of the nation, to control and
2 protect the external value of the national monetary
3 unit and to mitigate by its influence fluctuations in the
4 general level of production, trade, prices and employment,
5 so far as may be possible within the scope of monetary
6 action, and generally to promote the economic and
7 financial welfare of the Dominion". Debt management
8 has periodically hindered the Bank in carrying out these
9 functions.

10 31. The placement of new Government Canada issues
11 is carried out by a number of different methods, normally
12 through primary distributors including the Chartered
13 Banks, members of the I.D.A.C. and other brokers and
14 dealers. Most of these distributors do not normally
15 take positions or make markets in Government securities.
16 We contend that consideration should be given to reducing
17 the unwieldy list of primary distributors to those
18 who regularly operate in this field. In some new issues,
19 the amount being publicly offered is unknown due to
20 Government or Bank subscription. This causes uncertainty
21 particularly in view of the fact that such bonds may
22 be re-offered at a later date, since the adequacy of
23 the pricing and the judgment of the market's ability to
24 absorb an issue depends to a large degree on the size
25 of the issue. On occasion the Bank has acquired the
26 entire amount of a new issue at the advertised price
27 and subsequently sold the bonds to primary distributors
28 at a higher price. Such techniques are undesirable in
29 our view. To a considerable degree these unorthodox
30 activities have been necessitated by the Government's



of the economic life of the nation, to control and
protect the external value of the national monetary
unit and to mitigate by its influence fluctuations in the
general level of production, trade, prices and employment,
so far as may be possible within the scope of monetary
action, and generally to promote the economic and
financial welfare of the Dominion". Debt management
has periodically hindered the Bank in carrying out these
functions.

31. The placement of new Government Canada issues
is carried out by a number of different methods, normally
through primary distributors including the (named)
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and subsequently sold the bonds to primary distributors



1 heavy cash requirements.

2 32. The statistical material provided by the
3 Bank is invaluable to business and government. More
4 frequent publication of explanatory material would be
5 helpful.

6 33. The MacMillan report emphasized that the
7 Directors of the Bank should be men of experience, skill
8 and integrity. Our investigation indicates that less
9 than one-half of the man years served by the outside
10 Directors of the Bank have been served by men whose
11 background was related to financial business. In
12 the future more emphasis might be laid on the selection
13 of men with experience and skill in financial matters.

14 34. The Bank's most important function is to
15 influence economic conditions by effecting changes in
16 Chartered Bank cash positions. As important and related
17 objective is to broaden the market for Government
18 securities and the Bank has taken a number of forward
19 steps to increase the liquidity of the market. A
20 further step in the form of extending bank lending
21 facilities to selected dealers on collateral now beyond
22 the term of the money market might be explored.

23 35. Open market operations are a traditional tool
24 of implementing Central Bank monetary policy and these
25 operations are more effective if the securities markets
26 are broad and resilient (see definitions Appendix F).
27 The Bank can effect such operations by buying more or
28 less at weekly bill tenders as well as by operations
29 in the securities markets. At times the Bank seems
30 to have underestimated the psychological results of open



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1 market dealings. Since the bill sector of the market
2 is broad and resilient it seems logical that the Bank
3 should conduct its open market operations primarily
4 in the short term sector of the market. In periods
5 of crisis when disorderly markets may occur, there may
6 be occasional need for the Bank to transact business
7 in longer maturities.

8 36. In connection with Bank trading, it should
9 be pointed out that its traders in the financial centres
10 of Toronto and Montreal are not given sufficient
11 authority and discretion. Also, its trading departments
12 are understaffed. Although they will deal with all
13 dealers some pressure is removed from Bank traders
14 by virtue of the \$250,000 minimum on Bills and bonds
15 due within three years and a \$100,000 minimum on other
16 transactions. But consideration should be given to
17 limiting trading of the Bank to these organizations
18 which endeavour to make markets regularly.

19 37. The Bank of Canada is responsible for operating
20 Government accounts and funds such as the Securities
21 Investment Account, (which is used to invest surplus
22 Government cash) and the Unemployment Insurance Fund.
23 Operation of the latter has in the past frequently
24 necessitated buying or selling action which was
25 contrary to the Bank's monetary policy. Due to portfolio
26 changes in 1961, this is no longer such an important
27 factor. The Bank also operates The Purchase Fund
28 for the Government. The market has been unsettled
29 by the knowledge that securities in this and other funds
30 might be re-offered at any time. This trading can have



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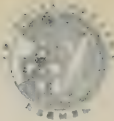
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1 important affects on the banking system and also can
2 be confused with open market operations and thus be
3 unnecessarily disquieting to the market.
4 38. When the Bank purchases or sells exchange,
5 it may contract or enlarge Chartered Bank reserves.
6 Until recently, exchange reserves have been sufficiently
7 steady that the Bank's operations in the exchange
8 market have had no significant effect on the Canadian
9 economy. Since the declaration of the Government
10 Exchange Policy in 1961, substantial changes in this
11 fund have occurred. Dislocations in the exchange
12 market have resulted. A full examination of this area
13 of the Bank's responsibilities and operations would
14 be desirable at this time.

15 39. Since 1954, the Bank has had the power of
16 regulating the cash reserves of the Chartered Banks
17 and since 1955 secondary reserves have been required.
18 It would seem that the agreement that requires
19 secondary reserves is now at best of doubtful value.

20 40. Traditionally changes in the discount rate
21 signal changes in the intention of the Central Bank
22 and touch off adjustments through the entire interest
23 rate structure. To our knowledge, Canada is the only
24 country where this is not true today. Because the
25 discount rate is tied to the bill rate, changes in
26 it have little psychological impact. While the Bank
27 can effect moves in the discount rate by buying or
28 selling Bills, other central banks employ both open
29 market operations and discount rate adjustments to
30 indicate their policies and intentions. It is suggested



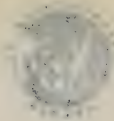
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1 that the Bank return to an administered rate.

2 41. The Bank's monetary policies would be more
3 effective if other institutions which accept deposits
4 and make loans were subject to regulations equally
5 effective to those which the Bank exercises over
6 chartered banks. It is further suggested that the
7 Commission consider whether powers should be given to
8 the Bank to influence margin requirements, terms of
9 instalment purchase, term lending by banks and cash
10 reserves of "near" banks. The Bank's ability to deal
11 with these sectors is at present largely dependent on
12 its powers and moral suasion. While most of its attempts
13 at suasion have been successful, occasionally its
14 objectives have not been attained. Failure in this
15 area can prove to be embarrassing.

16 42. Even under the most harmonious fiscal and
17 monetary politices, actions of the Bank can never
18 provide a perfect solution for Canada's economic
19 problems. It can only act in a broad and general manner
20 to bring about an atmosphere more conducive to the
21 attainment of desirable economic objectives.
22 Occasionally, in the interests of orderly markets,
23 actions must be taken which tend to controvert
24 monetary policy. Bank effectiveness is severely limited
25 in periods where fiscal policy must take precedence
26 over monetary policy. The emphasis of the Canadian
27 economy on international trade implies that deficit
28 spending or expansionary monetary policy does not have
29 as strong an effect as many might expect. Such policies
30 have little influence on foreign demand for our products



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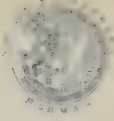


1 and indeed, in so far as they may influence costs and
2 prices, could even reduce this demand. On the other
3 hand, such expansionary actions are dissipated to a
4 considerable degree by substantial imported goods.
5 With these limitations in mind it is urgent that
6 government return to fiscal orthodoxy as soon as
7 possible. Cyclically balanced budgetary policy is
8 needed to bring fiscal and monetary policies back into
9 harmony.

10
11 MUNICIPAL FINANCE - Appendix D

12 43. The Canadian municipality is responsible
13 for matters which primarily affect local residents.
14 While education is considered a provincial responsibility,
15 facilities and teachers are provided by the municipality.
16 Municipalities owe their existence and authority to the
17 provinces. The special sphere of operations of the
18 municipality necessitates discussing its capital
19 financing separately from provincial finance.

20 44. The municipality's basic sources of capital
21 are current revenues, grants from senior governments
22 and the proceeds from the sale of debentures. The
23 rapid population growth since 1945 combined with the
24 demand for higher standards of services has resulted
25 in increasing municipal capital requirements. In some
26 provinces, provincial corporations have been established
27 to buy municipal debentures and in some others annual
28 grants covering a percentage of annual service charges
29 on debentures are provided. Such assistance has
30 aided municipalities in obtaining their capital require-



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ments and in holding down their borrowing costs.

45. The traditional method for a municipality to raise capital is by selling debentures. Normally, the established municipality with a moderate capital borrowing programme will achieve good results by calling for tenders. However, a municipality with a heavy borrowing programme may be well advised to market issues through a fiscal agency group. Cities such as Ottawa, Hamilton, Vancouver and Toronto have followed this practice from time to time. Fiscal agencies may also be best suited for new municipalities and those in special circumstances or difficulties. A fiscal agency ensures that issues are properly prepared and well marketed. Sometimes calls for tenders are sent to only a small list of dealers. Such notices should be published in an official gazette so that all dealers will have an opportunity to tender. In general the bid that provides capital at the lowest cost should be accepted.

46. Municipal debentures are evaluated by comparing them with the issues of other borrowers. This comparison necessitates a lot of information and statistics. Of prime importance are information and statistics which will display the quality and diversity of assessment, the tax collection record, the weight of the debt and the debt history. Comparison is made difficult by the variety of bases of assessment and statistical information from province to province. Standardization on a nation-wide basis would be very helpful in evaluating municipal credits. In addition



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1 to the basic evaluation the investment dealer must
2 consider such features as term, redemption clauses
3 and coupon rates.

4 47. The chief markets for municipal debentures
5 are financial institutions such as the chartered banks
6 and trust companies which favour purchasing the shorter
7 maturities and the insurance companies and pension
8 funds which favour purchasing the longer maturities.

9 Capital requirements of Canadian municipalities in
10 1961 were estimated at \$471 million or about 46.5 per
11 cent of total provincial financing in that year.

12 Since the imposition of the 15 per cent federal with-
13 holding tax practically all of the capital requirements
14 have had to be raised in Canada. This has denied
15 municipalities the advantageous rates which were being
16 obtained on external borrowings and tended to increase
17 borrowing costs. Consideration should be given to
18 rescinding this withholding tax.

19 48. Marketing of issues would be assisted if
20 municipalities would refrain from offering true serials
21 which result in odd principal amounts that are difficult
22 to sell. In general, serials are difficult to sell to
23 the public because there are so many different maturities.
24 in the early years designed for sale to the banks and
25 others, and a long term sinking fund maturity to
26 satisfy the requirements of other institutions and the
27 public. Sinking funds would create some demand for
28 outstanding debentures and assist in making a market.
29 The market for municipal issues would also be improved,
30 if the Department of Insurance were to permit insurance



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48. Marketing of issues would be assisted if municipalities would refrain from offering those series which result in odd principal amounts that are difficult to sell. In general, series are difficult to sell to the public because there are so many different maturities in the early years designed for sale to the banks and others, and a long term sinking fund maturity to satisfy the requirements of other institutions and the public. Sinking funds would create some demand for outstanding debentures and assist in making a market. The market for municipal issues would also be improved if the Department of Insurance were to permit insurance



1 companies to evaluate their holdings at the amortized
2 book values as is the practice for federal and
3 provincial obligations. Also, school debentures should
4 be made eligible for deposit by non-resident insurance
5 companies. In our opinion the issuance of tax exempt
6 debentures in Canada would not result in a substantial
7 improvement in the market or in significantly lower
8 debt service charges.

9 49. The provinces have been increasing their
10 assistance to municipalities. A simple but effective
11 form of assistance is to require municipalities to
12 provide the provinces concerned with information about
13 their history and economic and financial condition.
14 The provinces then distribute the information to dealers
15 and very often incorporate it in tender notices.
16 Another effective method of assistance is for the
17 province to remit certain grants to the paying agents
18 for the debentures so that these grants may be used
19 directly in servicing the debt. This procedure has
20 resulted in lower borrowing costs for the municipality.
21 The market for municipal debentures has been assisted
22 by purchase of parts of issues by various provincial
23 accounts, but probably the most effective form of
24 marketing assistance is the provincial guarantee of
25 principal and interest payments. This is undoubtedly
26 of major importance in marketing of issues of little
27 known or low rated municipalities and school boards.



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CORPORATION FINANCE AND LEGISLATION - Appendix E

Corporation Finance

50. During the 10 years, 1949 - 1959, the number of companies tabulated by the Department of National Revenue rose from 35,706 to 86,996 and their assets from \$21 billion to \$63 billion. There are several assumptions which should be kept in mind in using these statistics but subject to these, 38 per cent of the application of funds of these companies over the period was derived from long term debt and equity issues. For the capitalization of the finance and utility segments of this group debt is a higher proportion of the total. In the manufacturing sector 60 per cent of the funds were generated internally, 12 per cent from the issuance of debt, 14.5 per cent from equities and 13.5 per cent from other sources. Over the 10 year period this tabulation showed capital expenditures of \$11 billion with capital cost allowances contributing \$6.7 billion or about 60 per cent. Reflecting this large contribution of internally generated funds, the working capital ratio of the group declined only slightly from 3:1 in 1949 to 2.7:1 in 1959. The percentage of debt in the capitalization increased from 12 per cent to 17 per cent. The trend towards higher proportion of debt in the capital structure was particularly evident in the case of smaller companies where there is a strong desire not to dilute ownership and to achieve leverage. Smaller firms also showed a noticeably higher proportion of bank borrowings in their capital structure.



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1 51. It is important to note that the cost of
2 issuing debt in the post-war period has been lower than
3 the cost of raising funds through issue of preferred
4 and common shares. A rising corporation tax rate is
5 responsible for this and the higher this rate the
6 greater is the cost differential. At today's rate a
7 company can afford to pay an interest rate of 8 per
8 cent before the net cost exceeds a dividend rate of
9 4 per cent. At a 40 per cent corporate tax rate the
10 interest-rate-equivalent of 4 per cent dividend would
11 be reduced to 6.7 per cent. The pronounced tendency
12 of corporate income tax rates to creep upward provides
13 positive incentive for unsound corporate financing.
14 The financial structure of companies varies according
15 to size. Small companies tend to have more recourse
16 to bank and mortgage financing and to retain a higher
17 proportion of profits. These differences reflect
18 the ease with which large companies can obtain funds
19 in the market.

20 52. Data published by the Bank of Canada on new
21 issues of securities from 1949 - 1960 shows a total of
22 \$8.8 billion being raised, of which \$5.2 billion was
23 debt, \$.6 billion preferred, and \$3.0 billion common.
24 Rights issues of the chartered banks and the Bell
25 Telephone accounted for 28 per cent of the total new
26 issues of common stocks. The proportion represented
27 by debt varied from year to year but in the 1949 - 1956
28 period was 56.3 per cent and for the 1959 - 1960 period
29 59.5 per cent of the total. During the period of this
30 survey a number of new large companies were formed,



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Date published by the Bank of Canada on new issues of securities from 1949 - 1960 shows a total of \$8.8 billion being raised, of which \$5.2 billion was debt, \$1.6 billion preferred, and \$2.0 billion common. Rights issues of the chartered banks and the Bell Telephone accounted for 28 per cent of the total new issues of common stocks. The proportion represented by debt varied from year to year but in the 1949 - 1956 period was 26.5 per cent and for the 1959 - 1960 period 29.5 per cent of the total. During the period of this survey a number of new large companies were formed.



1 notably natural gas utilities and finance companies
2 and some large firms were absorbed by others, notably
3 in the pulp and paper industry. Thus, the total number
4 of public companies did not increase very substantially.
5 Indeed, between the end of 1948 and the end of 1961,
6 the number of stocks listed on the T.S.E. increased only
7 from 867 to 1,117 with most of the increase being in
8 the junior mining and petroleum group.

9 53. A detailed description of the underwriting
10 process in Canada is provided in Appendix E Paragraphs
11 17 to 34. In addition, the dealer often acts as agent
12 for the issuer in privately placing securities with
13 institutions. Lower commissions are charged for
14 private placements as the expenses and risks are much
15 lower. Occasionally, small issues are underwritten on
16 a "best efforts" basis with the dealer receiving a
17 straight commission on the sales made. A major
18 underwriter has the responsibility of providing sound
19 advice on the best terms and lowest overall costs of
20 an issue. He must also provide the placement power
21 to sell the issue, and, in doing this, must correctly
22 represent to his clients the quality of the issue and
23 the degree of risk.

24 54. A study of the distribution of holdings
25 of corporate and other non-Government bonds indicates
26 that domestic institutions and pension funds provide
27 the largest market. Among this group the life insurance
28 industry is the most important buyer. In 1954 this
29 industry held approximately 35 per cent of the outstanding
30 total amount of these bonds but by 1959 this had declined

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1 to 29 per cent. This trend indicates that problems
2 of distribution are becoming more complex and that the
3 investment dealer is having to develop other markets.
4 55. The cost of issuing securities varies with
5 the size of the issue and the degree of risk. Legal
6 fees, prospectus preparation and production, research
7 and sales expenses are more or less fixed regardless
8 of the size of the issue. Risks are greater on
9 securities of small or new companies. Both the risk
10 and expense factors mean higher costs on small issues.
11 Comparison of figures in tables 4 and 5 (Appendix E)
12 which show Canadian and S.E.C. data, indicate that
13 underwriting cost of small issues under \$3 million are
14 lower in Canada than in the U.S. and somewhat higher
15 on issues over this amount. A Moody's study of U.S.
16 utility issues shows spreads of from .10 per cent to .17
17 per cent while issues of Canadian utilities with similar
18 ratings showed spreads ranging from .11 per cent to .17
19 per cent. Despite these similarities there are
20 fundamental differences between the two markets. The
21 size of the financial institutions in the U.S. is such
22 that large issues can be sold to a small number of
23 buyers, whereas in Canada most issues are sold to a
24 large number of institutions and individuals. This
25 means that costs of distribution are significantly
26 higher in Canada.
27 56. Utilities in the U.S. are required to call
28 for competitive bids, whereas in Canada the practice
29 is to have negotiated issues. In theory competitive
30 bidding might be expected to produce the most favourable



CHAPTER IV
THE COST OF ISSUING SECURITIES

of distribution are becoming more complex and that the investment dealer is having to develop other markets.

55. The cost of issuing securities varies with the size of the issue and the degree of risk. Legal fees, prospectus preparation and production, research and sales expenses are more or less fixed regardless of the size of the issue. Risks are greater on securities of small or new companies. Both the risk and expense factors mean higher costs on small issues. Comparison of figures in tables 4 and 5 (Appendix B) which show Canadian and U.S.C. data, indicate that underwriting cost of small issues under \$5 million are lower in Canada than in the U.S. and somewhat higher on issues over this amount. A Moody's study of U.S. utility issues shows spreads of from .10 per cent to .17 per cent while issues of Canadian utilities with similar ratings showed spreads ranging from .11 per cent to .17 per cent. Despite these similarities there are fundamental differences between the two markets. The size of the financial institutions in the U.S. is such that large issues can be sold to a small number of buyers, whereas in Canada most issues are sold to a large number of institutions and individuals. This means that costs of distribution are significantly higher in Canada.

56. Utilities in the U.S. are required to call for competitive bids, whereas in Canada the practice is to have negotiated issues. In theory competitive bidding might be expected to produce the most favourable

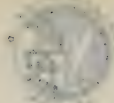


1 prices but there is reason to believe that this may
2 not be true. In a survey of 16 comparable pairs of
3 issues, 11 of the comparisons showed a yield to the
4 public and yield cost to the company to be lower for
5 negotiated sales. The fiscal agent maintains a
6 continuous relationship to the Company and is in a
7 position to assist in determining the timing and terms
8 of an issue. He can also test the market ahead of time
9 which is a distinct advantage. In competitive bidding
10 dealers are required to bid on short notice without
11 the benefit of advanced preparation and full and
12 detailed knowledge of the Company's position and
13 therefore, they tend to allow for unforeseen contingencies.
14 On this subject Judge Medina has commented that the
15 advantages to an issuer of a continuing relationship
16 with a good investment banker are obvious.

17 57. Canadian companies either gradually write
18 off expenses and discounts on issues, or charge them
19 at once to earned surplus. These charges are not
20 deductible for income tax purposes. To the extent that
21 these charges represent underwriters' commission we
22 feel strongly that they should be a deductible item
23 as they are a cost of raising funds.

24
25 Legislation

26 58. Securities legislation in Canada involves
27 10 provincial securities acts, various provincial
28 companies acts, the Companies Act of Canada, the Ontario
29 Corporations Information Act and the Quebec Companies
30 Information Act. There has been a movement toward



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Legislation

58. Securities legislation in Canada involves 10 provincial securities acts, various provincial companies acts, the Companies Act of Canada, the Ontario Corporations Information Act and the Quebec Companies Information Act. There has been a movement toward



1 achieving uniformity in this mass of legislation which
2 movement has been encouraged and endorsed by the IDAC.
3 The provinces are currently studying a uniform Companies
4 Act and 4 provinces now have identical or nearly identical
5 securities acts. There would seem to be large advantages
6 to the investing public and the investment industry
7 in enacting uniform securities legislation and adminis-
8 tering it in a uniform manner. In the U.S. there are two
9 Federal acts and in addition 48 states also have securities
10 legislation. It would seem likely that if SEC-type
11 legislation were established in Canada it would not
12 replace existing provincial statutes but would be
13 superimposed on these. The Association believes that
14 such superimposition would not in the best interests
15 of our capital market.

16 59. It would seem desirable that the various
17 securities acts should permit the production and
18 distribution of a preliminary prospectus in Canada
19 as is the practice in the United States. This would
20 permit more orderly marketing of new issues and give
21 security purchasers more time in which to study them.
22 It would also be helpful if all regulations affecting
23 the underwriting and sale of securities were promulgated
24 to the I.D.A.C.

25 60. The I.D.A.C. has strongly asserted that in
26 the interests of justice provision should be made for
27 arbitration and independent appraisal by provincial
28 governments desiring to expropriate electric utilities.
29 It would seem desirable that the temptation to
30 expropriate arising out of the Federal tax treatment



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1 of the provinces should be removed. Also, certain
2 mergers and amalgamations may be beneficial to Canada
3 but the I.D.A.C. deplores certain recently employed
4 "take-over" techniques.

5 61. A company incorporated under the Companies
6 Act of Canada is a natural vehicle to carry on business
7 in several provinces. However, this Act contains
8 several anomalies which tend to deter incorporation
9 and to create unnecessary delays and expenses. This
10 Act should be reviewed with a view to eliminating
11 these anomalies.

12
13 THE SECONDARY BOND MARKET - Appendix F

14 62. Through the secondary market, previously
15 issued securities are transferred from one investor
16 to another. Those normally participating in this market
17 are Bank of Canada, chartered banks, Members of the
18 I.D.A.C. and a number of other brokers and dealers.

19 63. The secondary market is large and active
20 and absolutely vital providing a mechanism for invest-
21 ment and dis-investment. In 1961 the volume of sales
22 of I.D.A.C. members, exclusive of primary market sales,
23 \$15.9 billion and their average quarterly inventories
24 were \$337.6 million (see table 1 appendix F). This
25 active market ensures liquidity and establishes a
26 spectrum of values. The substantial difference
27 between mortgage and bond rates is primarily the
28 result of the liquidity provided by the secondary
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1 Canada and the dealings of the various Government
2 accounts.

3 64. Up to 1917, the markets for Canadian debt
4 securities were concentrated in London and New York.
5 The large Government financing of the First World
6 War and the corporate financing of the 1920's
7 necessitated and encouraged the growth of a highly
8 developed secondary bond market.

9 65. The Trading Departments of many dealers
10 are regarded as the nerve centres of their operations.
11 Vast networks of private wires, telephones and other
12 public services are utilized to maintain contact with,
13 and to trade in, national and international markets.
14 These networks enable the industry to give adequate
15 service from coast to coast and literally to draw
16 upon the savings of the nation.

17 66. A number of dealers customarily act as
18 principals and their willingness to assume liabilities
19 in accordance with future trends of the market, as they
20 judge it, does much to moderate market swings. The
21 positions they take also permit trading in the size
22 required by insurance companies, banks and other
23 institutions. Some 30 to 40 dealers make markets
24 in the vast majority of the securities traded, do
25 the bulk of the trade and carry most of the inventory.
26 These are the dealers to whom financial institutions,
27 the Bank of Canada and other dealers look for prices,
28 bids and offerings. The ability of these dealers
29 to provide trading services would be improved if
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1 practice of lending bonds at reasonable rates.

2 67. ~~James~~ Secondary market trading in debt securities

3 has not attracted restrictive legislation as the

4 industry has demonstrated its competence in self

5 regulation. This is primarily due to the regulation

6 provided by the I.D.A.C. and Bond Traders' Associations,

7 which is described in detail in Appendix A part 1.

8 The occasional misunderstandings and difficulties

9 which have occurred have been dealt with quickly

10 and responsibly by the industry's regulatory bodies.

11 68. ~~James~~ The secondary bond market is customarily

12 divided into two categories, one being the money market

13 which is dealt with in Appendix G and the other

14 consisting of all other securities, principally those

15 maturing beyond three years. It is important that a

16 broad and resilient market exist at all times for

17 Government of Canada medium and long term bonds

18 because these bonds provide the bench mark from which

19 all other securities are graded. Investors look to

20 the market for Government of Canada bonds for

21 stability, quality and marketability. However, except

22 for artificial support provided by the Government

23 the long term Canada market has not had depth in recent

24 times. For Provincial issues, the market tends to be

25 narrower although the large issues of Ontario and Quebec

26 receive broad public interest. In general, municipal

27 bonds have limited secondary markets, and, except for

28 the largest corporations, the supply of corporate

29 bonds usually dries up shortly after new issues.

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1 from the keen competition between dealers and provides
2 all investors with access to fair prices.

3 69. A characteristic of a growing economy in the
4 large demand for funds in relation to the supply.

5 The U.S. market is now the major source of foreign
6 funds. It is therefore necessary for Canadian interest
7 rates to be higher than comparable U.S. rates if funds
8 are to be attracted to Canada.

9 70. The most significant domestic factors
10 affecting interest rate trends in Canada, are the
11 Federal Government's fiscal policy and the monetary
12 policy of Bank of Canada. A fiscal policy, even on
13 a long term cyclical basis, of balancing deficits
14 with surpluses would provide a strong underpinning
15 to the whole bond market. The recent policy of
16 utilizing Canada Savings Bonds as a prime method
17 of financing has tended to reduce the number of
18 private investors buying bonds without redemption
19 privileges. This is adversely affecting the breadth
20 of the long term bond market.

21 71. Policies which will increase confidence in
22 Federal Government securities are of major importance
23 in stabilizing markets and in the long run, in improving
24 the general functioning of the economy. Such policies
25 include: determined effort to balance the budget and
26 re-examination of the tax structure. The establishment
27 of a specific month for the Budget Address and regular
28 reports on the Government's financial policies would
29 remove some of the uncertainties from the market.

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2 such as the return to a stated rediscount rate, should
3 be considered. Uncertainty could be reduced by more
4 rapid replies to dealer bids and offerings by Bank of
5 Canada. This institution is the most important single
6 influence in the market and its actions should be
7 quick and decisive. It might be desirable to remove
8 portfolio dealings for Government accounts from Bank
9 of Canada jurisdiction and also to have the Bank play
10 a lesser part in the subscription for new issues.
11 Actions by Bank of Canada should reflect monetary
12 policy not agency trading. Thus, through modifying
13 its trading practices and through regular policy
14 explanations, the Bank could better guide the market.
15 73. The last section of Appendix F deals with
16 the advantages and disadvantages of a bond exchange
17 and concludes that the present dealer market provides
18 with the most efficient service at the lowest cost.

19
20 "SHORT-TERM MONEY MARKET" - Appendix G

21 74. The money market, which began in 1954
22 when thirteen dealers were granted lines of credit
23 has grown substantially since that time. This growth
24 can be seen in the variety of borrowers presently
25 competing for the available short-term funds and in
26 the tremendous growth in volume since that time.
27 This competition for credit and the rates offered have
28 attracted many who had previously left them lying dormant
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1 term interest rates which occurred in 1959 did much
2 to make investors sware of the substantial rewards
3 of making their cash work at all times.

4 75. An increasing number of borrowers are raising
5 part of their capital requirements in the short-term
6 market. The Federal Government, since the Conversion
7 Loan of 1958, has raised nearly all of its cash in
8 the money market. The longer maturities issued by
9 the government (excluding C.N.R.'s) during this time
10 were all, with the exception of one issue, sold to
11 the Bank of Canada for resale to the public.

12 76. Provincial and municipal governments have
13 also found that the money market will provide them
14 with additional sources of funds at a relatively low
15 cost, while often allowing them to choose the most
16 favourable time for financing in the long-term market.
17 Finance companies regularly borrowed a considerable
18 part of their requirements in the short-term market,
19 but over the past five years, corporations have also
20 become active sellers of paper. Because of these
21 developments in the money market, the chartered banks
22 and trust companies have been forced to become more
23 aggressive in retaining deposits and in attracting
24 new deposits.

25 77. At the present time, few statistics relating
26 to the money market are collected and made available
27 to the public. The Bank of Canada publishes the amount
28 outstanding and distribution of treasury bills and short-
29 term government bonds two years and under. The Dominion
30 Bureau of Statistics supplies information relating to



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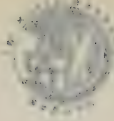
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1 the short-term borrowings made directly by the provinces.
2 However, there is no information available as to the
3 amount of municipal borrowing in the money market
4 or of the amount of corporate paper issued and out-
5 standing. It is recommended that more detailed statistics
6 be kept relating to all sectors of the money market.
7 Appendix G examines in some detail the amounts of
8 various short-term obligations presently outstanding
9 in the market, i.e., (a) treasury bills, (b) Government
10 of Canada and Guaranteed bonds maturing within three
11 years, (c) provincial and municipal short-term
12 obligations, (d) sales finance company paper,
13 (e) corporate paper, (f) deposits accepted by the
14 banks and trust companies.

15 78. The Floating Bank Rate, calculated weekly
16 at $\frac{1}{4}$ of 1 per cent above the average rate paid for
17 91-day Treasury Bills, plays a practical and
18 stabilizing role in the money market. The variable
19 Bank Rate has encouraged the money market dealers
20 to carry on inventory of government securities during
21 periods of cash adjustment in the banking system, when
22 day-loan facilities are not available. If the Bank of
23 Canada returns to a traditional Bank Rate, it is
24 recommended that a "Bank Accommodation Rate" or "Bank
25 Lending Rate" be made available by the Bank of Canada
26 to the money market dealers on a formula similar to
27 the present Floating Bank Rate.

28 79. The money market dealers have developed an
29 efficient market capable of transferring large amounts
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The money market dealers have developed an efficient market capable of transferring large amounts of short-term securities at narrow price spreads, and



1 the initial problem of two financial centres in Toronto
2 and Montreal has been largely overcome. However, the
3 Bank of Canada's trading departments in Toronto and
4 Montreal, which are the Bank of Canada's contacts
5 with the market, are not mechanically equipped nor
6 staffed to handle the practical problems relating
7 to the money market. The dealer at present frequently
8 finds it difficult to contact the Bank of Canada quickly
9 and receive immediate answers. These problems could
10 be largely overcome if the Bank of Canada's traders
11 had direct keys to the money market dealers and
12 Chartered Banks. It would also help if there was one
13 trader in each of the two cities who concentrated on
14 money market securities and had time to acquaint
15 himself with all the factors influencing the money
16 market rates.

17 80. The increasing role of the "country banks"
18 in financing dealer inventory is an important develop-
19 ment in broadening the money market. The I.D.A.
20 obtains statistics weekly from its members relating
21 to the amount of inventory financed away from the
22 chartered banks. This information is made available
23 to the members of the Association, Bank of Canada
24 and the Department of Finance.

25 81. At times, when the short-term rate
26 differential between the United States and Canada is
27 attractive to the non-resident, considerable funds
28 flow into the Canadian money market. Since the
29 introduction of the 15 per cent withholding tax on
30 treasury bills on December 20, 1960, these flows

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1 have been directed towards the purchase of Canadian
2 finance company and corporate paper. Canadian short-
3 term investors will themselves place funds in the
4 United States or abroad when rates are attractive.
5 The question of withholding taxes on money market
6 securities is dealt with in Appendix G. It should
7 be pointed out that nearly all non-resident short-term
8 investments are fully hedged. However, this is a factor
9 influencing Canadian foreign exchange rates and, at
10 times, money market rates, themselves, in Canada.

11 82. Our well-developed money market is
12 contributing substantially to Canada's economic growth
13 and the investment dealer organization has expanded
14 to keep pace.

15
16 CHARTERED BANKS AND "NEAR BANKS" - Appendix H

17 83. The relationships between the investment
18 dealer and the chartered banks and "Near Banks" are
19 discussed in Appendix H. "Near banks" are defined
20 as all institutions other than banks which receive
21 deposits or make loans.

22 84. The nature of the investment business is such
23 as to require continuous large scale accommodation
24 from these institutions by way of call loans and day
25 loans. Such loans are of high quality. During certain
26 periods and particularly during the period from
27 August 10, 1959 to October 11, 1960, chartered bank
28 rates on such loans remained unacceptably rigid.
29 Due to this lack of flexibility, ~~dealers~~ turned to "Near
30 Banks" for accommodation. This development arose purely



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INVESTMENT BANKING AND FINANCIAL INSTITUTIONS - APPENDIX H

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1 out of the need for a more competitive "price" on the
2 large borrowings of this industry. We believe that
3 the inflexibility of bank rates is in part caused by
4 the 6 per cent ceiling. This ceiling does not apply
5 to "Near Banks". It is recommended that the 6 per
6 cent limitation be removed to permit the chartered
7 banks more freedom to use a "price" basis as a deterrent
8 to undesirable loan expansion.

9 85. Investment dealers use the facilities of
10 banks extensively for deliveries and the like.

11 Co-operation between the I.D.A.C. and the C.B.A.
12 through the establishment of a joint committee would
13 smooth out imperfections in this area.

14 86. Banks are the custodians of the bulk of the
15 personal savings deposits of millions of Canadians.

16 The bulk of bank security holdings mature within a five-
17 year period and tend to be regarded as the temporary
18 utilization of idle resources. Thus these holdings
19 are very volatile, falling as commercial loans expand
20 and rising as commercial loans decline. The possibility
21 that personal savings deposits might be applied to a
22 greater degree to long term security holdings and thus
23 make a greater contribution to the economic growth
24 of Canada should be explored.

25 87. The chartered banks through term deposit
26 receipts are important issuers of securities. In our
27 opinion rate changes on these securities have not been
28 as responsive to changes in market conditions as is
29 desirable.

30 88. Chartered banks compete with dealers in the



...the ...
...the ...
...the ...

to "Near Banks". It is recommended that the 6 per

cent limitation be removed to permit the chartered

banks more freedom to use a "prime" basis as a deterrent

to undesirable loan expansion.

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87. The chartered banks through term deposits

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opinion rate changes on these securities have not been

as responsive to changes in market conditions as is

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1 underwriting and distribution of securities. They
2 are offered Government of Canada new issues on the same
3 terms as are dealers. One or more banks are part of
4 most syndicates bidding on new provincial issues.
5 The judgment of the bank in this area carries special
6 weight because it may also be a financial advisor to
7 the Province. Banks are frequently members of
8 syndicates bidding for Municipal issues, and, in the
9 case of serials, often agree to purchase the early
10 maturities. A bank's interest in the "shorts" has an
11 important effect on the price the syndicate is willing
12 and able to pay. In corporate issues bank participation
13 is infrequent. However, there are a few important
14 exceptions.

15 89. ~~and~~ Considerable disagreement exists amongst
16 our members as to whether bank participation in
17 syndicates is in the public interest or serves any
18 useful purpose. Some members believe that banks have
19 a generally salutary effect by sharing the risks,
20 providing accommodation, and by adding strength to
21 the bids by buying for their own account portions of
22 the issue. Others point out that undesirable conflicts
23 of interest may arise as a result of bank participation
24 and suggest that the primary function of banks is and
25 should continue to be the provision of short term
26 accommodation for their customers. The majority of
27 our members do agree that involvement of banks in
28 syndicates underwriting corporate securities should not
29 be extended. It should be recognized that satisfactory
30 performance of underwriting function is one of the



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1 principal contributions the investment dealer has to
2 offer to the proper functioning of the whole capital
3 market.

4 90. In distributing securities, banks enjoy
5 advantages resulting from their widespread branch
6 systems and special knowledge of customer resources.
7 They have been a significant factor in the distribution
8 of Canada Savings Bonds which we might point out involves
9 no risk and is done at only incidental cost. Banks
10 participate in selling groups on the same basis as
11 dealers. The effectiveness of banks in distributing
12 securities in small communities largely beyond the
13 reach of investment dealers is acknowledged. However,
14 important conflicts of interest can occur and at
15 times-individual bank managers may be inclined to
16 discourage investment in order to maintain savings
17 deposits. At such times as the banks are sellers of
18 securities to meet expanding demands for loans it is
19 particularly important that dealers have a strong
20 sales force to handle the essential function of
21 distribution.

22 91. As a result of the inadequacy and cost of
23 chartered bank accommodation at various times, dealers
24 have developed "near banks" as a source of funds.
25 These institutions also provide funds for other
26 financial intermediaries. They also issue a variety
27 of securities. The size and importance of these
28 institutions has grown in recent years and they have
29 a significant impact on the market place.
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1 RETAILING BONDS AND STOCKS and RISK CAPITAL - Appendix I

2 Retailing Bonds and Stocks

3 92. Bond sales up to the 1st World War were made
4 primarily in foreign markets with domestic sales being
5 confined to financial institutions and wealthy individuals.
6 The Victory Loan issues of the War carried high interest
7 rates and tax advantages which encouraged individual
8 investment. During the 1920 - 1930 period almost \$6
9 billion was invested in capital goods and the proportion
10 of foreign capital drawn upon was considerably reduced.
11 In this period, individuals participated in the security
12 markets in an increasingly broad and active manner.
13 The wide acceptance of the Victory Bonds of the 2nd
14 World War was a result of educating a large selling
15 force. In this period, the Payroll Savings Plan was
16 developed. The Victory Loan campaigns of World War
17 I, were responsible for millions of Canadians owning
18 investment securities for the first time. Today
19 there are over two million individuals in Canada who
20 own Government of Canada bonds. These citizens are
21 a stabilizing and supporting factor in the bond market.
22 Continuation of the habit of thrift developed during
23 the war is maintained by an annual Canadian Savings
24 Bond campaign.

25 93. The small investor, whom we shall define
26 as having up to \$10,000 invested in securities, does
27 not normally have much knowledge of securities markets.
28 His investments are usually either exceedingly
29 conservative or extremely speculative. The small
30 size of his holdings severely restricts the degree of



SAVING BONDS AND STOCKS AND RISK CAPITAL - A

Retailing Bonds and Stocks

92. Bond sales up to the 1st World War were made primarily in foreign markets with domestic sales being confined to financial institutions and wealthy individuals. The Victory Loan issues of the War carried high interest rates and tax advantages which encouraged individual investment. During the 1920 - 1930 period almost \$5 billion was invested in capital goods and the proportion of foreign capital drawn upon was considerably reduced. In this period, individuals participated in the security markets in an increasingly broad and active manner. The wide acceptance of the Victory Bonds of the 2nd World War was a result of educating a large selling force. In this period, the Payroll Savings Plan was introduced. Individuals were responsible for millions of Canadians owing investment securities for the first time. Today there are over two million individuals in Canada who own Government of Canada bonds. These citizens are a stabilizing and supporting factor in the bond market. Continuation of the habit of thrift developed during the war is maintained by an annual Canadian Savings Bond campaign.

93. The small investor, whom we shall define as having up to \$10,000 invested in securities, does his investments are usually either exceedingly conservative or extremely speculative. The small size of his holdings severely restricts the degree of



1 diversification he can achieve. The small investor
2 is likely to be a good market for bonds but is unlikely
3 to be a good source of capital for sound new enter-
4 prises. The investment dealer solicits his business
5 and spends much time educating and assisting him.

6 94. The medium investor is an individual with
7 between say \$10,000 and \$100,000 invested in securities.
8 Quite often he is a professional or business man whose
9 income is substantial and growing. On the other hand,
10 the medium investor may be a retired person, a widow
11 or a dependent who has inherited capital. Generally,
12 this class of investor will be moderately well-informed
13 but will tend to rely heavily on the advice of the
14 investment dealer. The professional or business man
15 is often in a high income tax bracket and therefore
16 interested in capital appreciation. Much of the
17 educational effort of investment dealers and the
18 I.D.A.C. is aimed at the medium investor.

19 95. The large investor who has securities
20 investments of \$100,000 or more will normally be quite
21 well informed. The cost of doing business with the
22 large investor, relative to the return, is substantially
23 below that with other groups. He provides a good
24 market for all types of securities including stocks
25 in risk ventures.

26 96. Investment dealers service the retail market
27 by sending salesmen into the field. This is not true
28 of banks and stock brokers. To service retail accounts
29 it is of primary importance that the dealer have the
30 knowledge and resources to study and underwrite the



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1 securities to be offered. He must also have a force
2 of qualified salesmen, facilities to train these sales-
3 men and capital to carry them until they become
4 productive. The trainee will usually spend time in
5 each of the operating departments, attend sales
6 meetings, and complete at least one of the courses
7 offered by the I.D.A.C. The dealer also requires a
8 research department to supply salesmen with information
9 and guidance, accounting and trading departments and
10 a communication system. He may also engage in portfolio
11 supervision and underwriting. Through the I.D.A.C.
12 as well as through a broad variety of material he
13 may produce himself, the dealer contributes to
14 the education of the investing public. Provision of
15 all these services means that the cost of doing retail
16 business is high.

17 97. ~~restored~~ The dealer must acquire clients to expand
18 his business. Most new investors come to dealers
19 through referrals but, in addition, the dealer attracts
20 them through advertising and through approaching them
21 directly. However, in some provinces there are legal
22 restrictions regarding approaching prospective clients
23 at home except to sell Government Bonds and this can
24 have the effect of somewhat restricting the development
25 of new accounts.

26 98. ~~restored~~ It would be helpful if the Government of
27 Canada would give more consideration to the retail
28 market when establishing the terms of new bond issues.
29 Such consideration would provide a strong incentive
30 to broadening the market for Government and other

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1 securities in Canada.

2
3 Risk Capital

4 99. All types and variations of securities issued
5 for the development of new ventures must be defined
6 as risk capital. Basically, there are two types of
7 risk capital -- that for long term investment in
8 intelligent and seriously conceived new ventures, and
9 that for short term investment in risky securities
10 where quick profits are sought with little concern
11 for the ultimate outlook of the enterprise. Many retail
12 investors who do take an interest in well conceived
13 ventures are inclined to ignore the ultimate potential
14 and accept short term capital gains, if and when
15 available. Thus, the equity in these ventures tends
16 to shift from the public to institutions and foreign
17 investors. On the other hand, the public will hold
18 for long periods the securities of such enterprises
19 as established utilities. Dealers are continually
20 attempting to educate and interest individual investors
21 in the long term development of new enterprises.
22 Participation in such developments could be broadened
23 if the shares of an institution such as the Industrial
24 Development Bank were offered publicly. It is
25 recommended that tax advantages be provided to
26 encourage individual investment in risk ventures.
27 100. Raising long term risk capital is difficult.
28 The investment dealer must do a great deal of work,
29 sometimes on many companies, before he finds one of
30 the size and promise suitable for public offering.



the size and promise available for public offering. sometimes on many companies, before he finds one of The investment dealer must do a great deal of work, 100. Raising long term risk capital is difficult. encourage individual investment in risk ventures. recommended that tax advantages be provided to Development Bank were offered publicly. It is if the shares of an institution such as the Industrial Participation in such developments could be broadened in the long term development of new enterprises. attempting to educate and interest individual investor as established utilities. Dealers are continually for long periods the securities of such enterprises investors. On the other hand, the public will hold to shift from the public to institutions and foreign available. Thus, the equity in these ventures tends and accept short term capital gains, if and when ventures are inclined to ignore the ultimate potential investors who do take an interest in well conceived for the ultimate outlook of the enterprise. Many report where quick profits are sought with little concern that for short term investment in risky securities intelligent and seriously conceived new ventures, and risk capital - that for long term investment in Basically, there are two types of for the development of new ventures must be defined 99. All types and variations of securities issued



1 Then he must, through sales meetings, field trips and
2 the like, introduce this Company to his sales force.
3 This is an expensive and time-consuming process.
4 In order to protect clients, the underwriter must
5 continue to take an interest in and make markets for
6 the securities he has distributed. Where difficult
7 conditions develop, the dealer will endeavour to protect
8 his clients' capital by devoting a considerable amount
9 of time, and sometimes his own capital, to the restor-
10 ation of the enterprise to profitable operation.

11
12 STOCK BUSINESS - Appendix J

13 101. The stock business in Canada is largely
14 carried on through the five stock exchanges, with the
15 Toronto Stock Exchange and the Montreal Stock Exchange
16 handling the vast majority of the business. These
17 two exchanges listed a total of about 1,250 stocks
18 at the end of 1961, at a quoted market value of close
19 to \$62 billion. Of this market value, about \$31 $\frac{3}{4}$
20 billion consisted of stocks of foreign firms, mainly
21 large United States companies. Excluding these foreign
22 stocks, trading activity in 1961 represented about
23 8.6 per cent of the quoted market value of the
24 Toronto Exchange. If adjustment is also made for that
25 portion of the stocks which are closely held, trading
26 activity would have represented about 12.3 per cent
27 of the supply available to the market. In recent
28 years there has been a growing number of secondary
29 distributions of large blocks of stock.

30 102. Stock trading is done on an agency basis



CONFIDENTIAL

A. 10

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STOCK BUSINESS - Appendix 1

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1 with commission rates as set by the exchanges being
2 charged for buying and selling. Commission rates were
3 revised upward in 1945 and subsequent to this, changes
4 have been primarily modest upward revisions and re-
5 classifications. Demands for added services in the
6 post-war period have been such that the cost of
7 consummating stock business has risen rapidly.

8 103. A large over-the-counter market exists
9 in Canada but the main volume of trading in this market
10 consists of bonds and debentures, which are dealt with
11 in Appendix F. The stocks traded in the over-the-counter
12 market are primarily those of natural resource and
13 specialty companies. A large number of dealers operate
14 in this market, but except in periods of active
15 development of new industries, such as uranium, over-
16 the-counter activity is very small compared with that
17 in the United States.

18 104. The supply of stocks available to the investor
19 through new issues has been strongly influenced in the
20 post-war period by the large proportion of capital
21 expenditures which business has financed internally;
22 foreign financing; the lack of certain growth industries
23 in Canada, such as electronics; the growth of foreign-
24 owned subsidiaries in Canada; expropriation of utilities
25 by Governments; mutualization of insurance companies;
26 increases in the corporate tax rate which provide
27 incentives for debt financing and by inflation, which
28 also provide incentives for debt financing and by
29 inflation, which also provides incentive for debt
30 financing. In recent years only about two fifths of the



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104. The supply of stocks available to the investor through new issues has been strongly influenced in the post-war period by the large proportion of capital raised by foreign financing; the lack of certain growth industries in Canada, such as electronics; the growth of foreign-owned subsidiaries in Canada; expropriation of utilities by Governments; mutualization of insurance companies; increases in the corporate tax rate which provide incentives for debt financing and by inflation, which also provide incentives for debt financing and by inflation, which also provides incentive for debt financing. In recent years only about two fifths of the



1 new capital raised by corporations has come from equity
2 financing. On the other hand, the supply of new stock
3 issued has undoubtedly been increased by the 1954
4 revision of the Bank Act, which assisted the banks
5 in making rights offerings; the limited financial
6 strength of certain companies which necessitates equity
7 financing and by the need of utilities and other
8 companies to maintain their equity bases.

9 105. The demand for stocks can be broadly divided
10 into that arising from individual investors and that
11 from various institutions. There is considerable
12 overlapping however because some institutional demand,
13 such as that of the mutual funds, arises directly from
14 individual investment. In 1959, just over 9 per cent of
15 Canadian families and unattached individuals owned
16 stocks, with the primary incidence being in the higher
17 income brackets. A United States survey in June 1955
18 indicated that 8 per cent of United States family units
19 were stockholders. Thus the incidence of individual
20 stock ownership is probably very similar as between
21 Canada and the United States.

22 106. The information available on institutional
23 stockholdings varies widely from one institutional
24 group to another. In 1960, life insurance companies
25 held only about 2.2 per cent of their assets in preferred
26 and common shares although the statutory limits permit
27 15 per cent. A large portion of the stocks held were
28 foreign and at December 31st, 1960, only .96 per cent
29 of their assets were represented by Canadian common
30 stocks.



new capital raised by corporations has come from equity financing. On the other hand, the supply of new stock issued has undoubtedly been increased by the 1934 revision of the Bank Act, which assisted the banks in making rights offerings; the limited financial strength of certain companies which necessitated equity financing and by the need of utilities and other companies to maintain their equity bases.

105. The demand for stocks can be broadly divided into that arising from individual investors and that from various institutions. There is considerable evidence to show that the demand for stocks from such as that of the mutual funds, arises directly from individual investment. In 1952, just over 9 per cent of the total investment in Canadian securities was made by individuals, with the primary incidence being in the higher income brackets. A United States survey in June 1952 indicated that 8 per cent of United States family units were stockholders. Thus the incidence of individual stock ownership is probably very similar as between Canada and the United States.

106. The information available on institutional stockholdings varies widely from one institutional group to another. In 1960, life insurance companies and common shares although the actuary limits permit 15 per cent. A large portion of the stocks held were foreign and at December 31st, 1960, only .36 per cent of their assets were represented by Canadian common



1 107. Fire and casualty companies, on the other
2 hand, hold 7.2 per cent of their assets in Canadian
3 and foreign common and preferred shares, a considerably
4 higher portion than most other institutions.

5 108. Trust companies represent a very important
6 sector of the demand for stocks. Of their assets,
7 approximately 2.9 per cent was invested in preferred
8 and common stocks at the end of 1960. However, 85
9 per cent of trust company funds are administered funds
10 and on a large segment of these there is no published
11 information. It can be assumed that a significant
12 proportion of these administered funds are invested in
13 equities. In this connection, it is interesting to note
14 that in 1959 the personal trust accounts in United
15 States banks and trust companies were over 70 per cent
16 invested in equities.

17 109. Mortgage and loan companies, at the end of
18 1960, showed the book value of common and preferred
19 holdings at 5.1 per cent of their total assets.

20 110. Pension funds provide a well-documented area
21 of institutional investment. The asset distribution
22 of the plans of incorporated companies show that
23 equity holdings grew from \$53 million in 1952, or
24 7.4 per cent of assets, to \$239 million in 1960, or
25 12.3 per cent of assets. These industry plans made up
26 about three fifths of total trustee pension plans.
27 Their emphasis on equities is as striking as is the
28 lack of such emphasis in the investments of crown
29 corporations and Government agency pension funds. In
30 1960, the holdings of all trustee pension plans



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1 represented approximately 1.16 per cent of the value of
2 all listed common stocks. It is estimated that the amount
3 of common stock investments of all trustee pension
4 funds was \$50 million in 1960, or about 12 per cent
5 of net funds available for investment.

6 111. Investment companies of the open-end type
7 are easily the most important source of demand for
8 equities. Their net flow of funds into equities in
9 1959 is estimated at \$80 million. At the end of 1959,
10 the market value of Canadian stocks held by these
11 companies totalled \$472 million and represented about
12 2.28 per cent of the value of Canadian common stocks
13 listed at that time.

14 112. In the post-war period, the investment by
15 non-residents and non-resident institutions has had a
16 very important impact on the demand for equities.
17 At the end of 1958 the book value of the capital stock
18 of Canadian companies, owned by non-residents, amounted
19 to \$9.3 billion, of which \$6.8 billion represented
20 direct investments. It is estimated that non-resident
21 trading accounted for about one-fifth of the value of
22 the shares traded on Canadian exchanges in 1959.

23 113. In the 1955-1959 period, N.R.O. funds and
24 other foreign-owned portfolio purchasers acquired
25 \$887 million in Canadian securities. During the post-war
26 period, there was a steady rise in foreign interests
27 in manufacturing, oil, natural gas and mining and
28 smelting and a steady decline in the interests of
29 foreign investors in railroads and utilities. The
30 direct foreign investment has been based primarily on a



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direct foreign investment has been based primarily on a



1 desire to gain access to the Canadian market, access to
2 the Commonwealth market or access to natural resources,
3 the latter often being associated with vertical integra-
4 tion. It is probable that without massive foreign
5 participation, many of the developments so financed
6 would never have taken place. In terms of technology,
7 the contribution of non-residents is unquestioned.

8 114. It is important to observe that institutional
9 holdings of stocks are heavily concentrated in a short
10 list of well-known companies. While institutional
11 demand has been rising sharply in recent years,
12 particularly from investment companies and pension funds,
13 in general, Canadian institutions apply a smaller
14 percentage of their assets to equities than do their
15 American counterparts. While individual holdings of
16 equities appear to be similar in Canada and the United
17 States it is clear that Canadians' indirect participation
18 in the stock market through various financial inter-
19 mediaries is weak in comparison with the experience
20 in the U.S.

21 115. The role of investment management has become
22 increasingly important in the Canadian economy since
23 World War II. Both individual and institutional
24 investors have become more knowledgeable and more
25 demanding and investment dealers have experienced
26 consistent pressures to provide more information and
27 sophisticated analysis. The investment dealer has
28 responded to the demands of growing numbers of
29 university-trained analysts in institutions by
30 occasion of his research department and to the demands



desire to gain access to the Canadian market, access to

the latter often being associated with vertical integra-

tion. It is probable that without massive foreign

participation, many of the developments so financed

would never have taken place. In terms of technology,

the contribution of non-residents is unquestioned.

114. It is important to observe that institutional

holdings of stocks are heavily concentrated in a short

list of well-known companies. While institutional

demand has been rising sharply in recent years,

particularly from investment companies and pension funds,

in general, Canadian institutions apply a smaller

percentage of their assets to equities than do their

American counterparts. While individual holdings of

equities appear to be similar in Canada and the United

States it is clear that Canadians' indirect participation

in the U.S. market is much smaller than in the U.S.

market is weak in comparison with the experience

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investors have become more knowledgeable and more

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consistent pressures to provide more information and

sophisticated analysis. The investment dealer has

responded to the demands of growing numbers of

university-trained analysts in institutions by

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1 of individuals by expanding portfolio management and
2 advisory services. It is estimated that it requires
3 4-6 years to develop a university graduate to the
4 status of a recognized analyst at a cost of some
5 \$40,000 - \$50,000. This, in addition to the growing
6 need for information services and communications, has
7 greatly increased the cost of doing business.

8 116. Improvements in the quantity and quality
9 of the services offered, have been hampered to a consider-
10 able degree, by the difficulty of obtaining detailed
11 and regular information from Canadian corporations. In
12 recent years, fortunately, many companies have become
13 more public and investor relations conscious. There
14 has been a noticeable improvement in the quality of
15 annual reports and an increase in the number of
16 companies issuing quarterly and semi-annual reports.
17 For some companies and industries, further improvements
18 are still needed.

19 117. The rise of investment clubs in Canada
20 in the post-war period has been significant in develop-
21 ing public interest in stock ownership. These clubs
22 provide an opportunity for members jointly to study
23 securities, thus broadening their investment knowledge
24 as well as providing a means of investing personal
25 savings. Investment clubs do not yet have a great
26 impact on the market and the smaller ones often deal
27 in odd lots, which transactions are unprofitable to the
28 broker. Nevertheless, investment dealers have encouraged
29 them because of the contributions they are making to
30 broadening the market for securities. In this area,



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1 as in the area of its co-operation with the various
2 stock exchanges, the Investment Dealers' Association
3 has played an important role in encouraging public
4 interest in equities.

5
6 MUTUAL FUNDS - Appendix K

7 118. Mutual funds, whose antecedents are the
8 investment trusts of Great Britain, really began to
9 develop on this continent in 1924 with the formation
10 of Massachusetts Investors Trust and State Street Invest-
11 ment Corporation, the first of the open end investment
12 companies. Between 1927 and 1930, over 700 investment
13 trusts and holding companies were formed in the United
14 States, nearly all of which were of the closed end type.
15 Many of these concerns were highly leveraged and there
16 was much pyramiding of one investment company into
17 another with the result that many more or less collapsed
18 in the 1929 stock market crash and the ensuing depression
19 years of the 1930's.

20 119. In Canada, 49 investment companies, practically
21 all of the closed end type, were in operation at the end
22 of 1929 and had assets of some \$265 million. While
23 there were varying degrees of leverage there was very
24 limited pyramiding with the result that the Canadian
25 trusts were not as hard hit as their American counter-
26 parts in the 1929 panic. Most of them won through and
27 are in operation today.

28 120. Nevertheless, Canadian investors lost heavily
29 on the "investment trusts" and confidence in such
30 organizations died. Management, as applied to investments,



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1 was at a big discount and the public wanted no part
2 of it. Inherently, however, the individual of more
3 modest means still sought ways of investing to provide
4 a combination of diversification, ready marketability,
5 and, equally important, ways of establishing the
6 proper market for his commitment - a feature that had
7 been conspicuously absent from the closed end trusts.

8 121. Investor confidence in investment companies,
9 however, was slow in returning. The first open end
10 type of mutual fund in Canada was established in 1932,
11 but it was not until 1950 that a strong investor
12 preference for this type of fund began to appear. The
13 last ten years have seen a rapid growth in the number
14 and size of mutual funds. There are now 41 mutual funds
15 of significant size in Canada of which 24 are Canadian
16 owned, and hold essentially Canadian securities, four
17 are primarily Canadian owned, but specialize in foreign
18 securities, three are owned primarily abroad, but with
19 Canadian investments, and ten are non-resident owned
20 (N.R.O.) companies investing in Canadian stocks.

21 At the end of 1960 the total net assets of these funds
22 was \$900 million and at the end of 1961 was estimated
23 to be about \$1 billion. During the past ten years
24 closed end type funds have been comparatively static
25 while mutual funds have developed into an increasingly
26 important position in Canadian financial markets.

27 122. A typical mutual fund has a simple capital
28 structure consisting of redeemable special shares and
29 a small number of deferred shares. The latter are
30 held by the management group. Both classes of stock



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121. Investor confidence in investment companies, however, was slow in returning. The first open end type of mutual fund in Canada was established in 1932, but it was not until 1950 that a strong investor preference for this type of fund began to appear. The last ten years have seen a rapid growth in the number and size of mutual funds. There are now 14 mutual funds of significant size in Canada of which 24 are Canadian owned, and hold essentially Canadian securities, four are primarily Canadian owned, but specialize in foreign securities, three are owned primarily abroad, but with Canadian investments, and ten are non-resident owned (N.R.O.) companies investing in Canadian stocks.

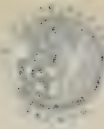
At the end of 1960 the total net assets of these funds was \$900 million and at the end of 1961 was estimated to be about \$1 billion. During the past ten years closed end type funds have been comparatively static while mutual funds have developed into an increasingly important position in Canadian investment.

122. A typical mutual fund has a simple capital structure consisting of redeemable special shares and a small number of deferred shares. The latter are held by the management group. Both classes of stock



1 have equal voting rights. The special shares, which are
2 redeemable at the holder's option, are sold to the
3 public at the net asset value which is calculated
4 daily, plus a loading charge of 8 per cent. Normally
5 the load is reduced to 5 per cent for purchase of over
6 \$50,000. The bulk of this charge is paid to the invest-
7 ment dealer or to the sales force of the underwriter.
8 A typical fund would be prohibited from borrowing
9 money, buying securities on margin or selling short.
10 Its investments would consist of about 70 common stocks
11 of well-known Canadian companies and about 15 per cent
12 of its portfolio would be in preferred stocks and
13 corporate bonds. A typical company would pay dividends
14 quarterly but would provide means for reinvesting
15 the dividends in the special shares of the fund. It
16 would be managed by a management organization which
17 would provide office space, administrative and research
18 staff and portfolio management services. The manage-
19 ment fee would be one-half of one per cent of the average
20 net asset value. Provisions would be made to ensure
21 arm's length dealing by the management.

22 123. Mutual funds are subject to Section 69
23 of the Income Tax Act and N.R.O. funds to Section 70.
24 Section 69 provides that investment companies pay a
25 tax of 21 per cent of their taxable income providing
26 they meet certain requirements, namely having at least
27 80 per cent of their property in, and 95 per cent of
28 their income from, securities or cash. At least 85
29 per cent of their gross revenue must come from
30 Canadian sources and not more than 25 per cent from



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1 interest. The fund must distribute in each yeat
2
3 at least 85 per cent of taxable income. Not more than
4 10 per cent of assets may be in the securities of one
5 corporation. In addition, it must have at least 50
6 shareholders, none of whom own more than 25 per cent
7 of the shares. The N.R.O. company, under Section 70,
8 is subject to a 15 per cent tax if at least 95 per cent
9 of its shares are held by non-residents; if not less
10 than 90 per cent of the gross revenues are from interest
11 or dividends; and if no revenue is derived from
12 business activities such as purchasing, merchandising,
13 manufacturing and the like.

14 124. Mutual fund shares are normally offered for
15 sale at their net asset value plus a fee or loading
16 charge. A few funds have a low loading and exact a fee
17 when shares are presented for redemption, but most funds
18 charge about 8 per cent on sales price and no fee for
19 redemption. Thus the loading covers both sale and
20 purchase. If the spread between bid and asked prices
21 of stocks traded on exchanges and the minimum
22 commissions which stock exchange numbers must charge
23 on small lots are taken into consideration, loading
24 charges do not appear to be excessive.

25 125. Mutual fund shares are offered for sale
26 through the fund management's own sales staff, through
27 investment dealers and through separate organizations
28 having their own sales staffs which are entirely
29 independent of the fund management. The shares may
30 be purchased as individual transactions and through



interest. The fund must distribute in each year

at least 85 per cent of taxable income. Not more than 10 per cent of assets may be in the securities of one corporation. In addition, it must have at least 50 shareholders, none of whom own more than 5 per cent of the shares. The N.R.O. company, under Section 70, is subject to a 15 per cent tax if at least 95 per cent of its shares are held by non-residents; if not less than 90 per cent of the gross revenues are from interest or dividends; and if no revenue is derived from business activities such as purchasing, merchandising, manufacturing and the like.

124. Mutual fund shares are normally offered for sale at their net asset value plus a fee on loading charge. A few funds have a low loading and exact a fee when shares are presented for redemption, but most funds charge about 8 per cent on sales price and no fee for redemption. Thus the loading covers both sale and purchase. If the spread between bid and asked prices of stocks traded on exchanges and the minimum commissions which stock exchange members must charge on small lots are taken into consideration, loading charges do not appear to be excessive.

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1 purchase plans under which a stated amount of money
2 is invested at regular intervals. The latter may be
3 on a voluntary or a contractual basis. Under the
4 contractual plans some mutual funds concentrate a
5 considerable part of the total load of the entire
6 contract into the initial years of the plan with the
7 result that if the purchaser terminates the contract
8 in the earlier years of its life he may only recover
9 part of the amount paid in. The great majority of
10 regular purchase plans are used by small investors
11 who contribute from \$15 to \$100 per month.

12 126. In 1957 the Income Tax Act was amended to
13 permit the self-employed person to contribute to an
14 individual retirement plan. Mutual fund shares qualify
15 as media for such plans and this feature has provided
16 a new and increasing outlet for their sales.

17 127. A number of funds provide "withdrawal plans"
18 whereby a shareholder may liquidate a portion of his
19 previously acquired block of shares at regular intervals.

20 This process is not in any way the equivalent of the
21 payment of an annuity and the shareholder has no
22 guarantee that his capital will not be exhausted.

23 While market experience over the past 11 years has been
24 favourable to most of these plans, there can be no
25 assurance or guarantee that this experience will repeat
26 itself. For the unsophisticated, the plan can appear
27 complicated and, unless explained by a highly
28 experienced salesman, misunderstandings could occur.

29 128. The growth of mutual funds may be regarded
30 as part of a broad trend toward equity investment by the

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1 public. Investment companies are media through which
2 the small investor can share in the risks and rewards
3 of equity investment while obtaining professional
4 management, broad diversification and liquidity. That
5 investors consider mutual funds attractive is illustrated
6 by the growth of five representative Canadian funds
7 which had assets of \$50 million in 1950 and \$555.5
8 million in 1961. (See Appendix K, Exhibit D.) It is
9 obvious that these funds have tended to promote
10 individual saving and encourage investment in equities.
11 Also, these funds have tended to make the small
12 individual investor more conservative in the sense that
13 they have attracted his interest away from highly
14 speculative commitments.

15 129. In Canada there is no special regulatory
16 legislation for investment companies although all mutual
17 funds are subject to the federal or provincial acts under
18 which they are incorporated as well as to the securities
19 acts of the provinces in which they sell their shares.
20 Mutual funds in Canada have to date voluntarily set
21 high standards of self-regulation. Nevertheless,
22 an examination of these acts should be made to ensure
23 that these provide adequate safeguards for the investing
24 public in both open and closed and investment trusts.

25
26 FINANCING SMALL BUSINESS. - Appendix L

27 130. Generally a worthwhile project requiring
28 \$500,000 or more can be financed with a debt or equity
29 issue. Small business requirements are therefore
30 defined as being less than this amount.



public. Investment companies are media through which the small investor can share in the risks and rewards of equity investment while obtaining professional management, broad diversification and liquidity. That investors consider mutual funds attractive is illustrated by the growth of five representative Canadian funds which had assets of \$50 million in 1950 and \$255.5 million in 1961. (See Appendix K, Exhibit D.) It is obvious that these funds have tended to promote individual saving and encourage investment in equities. Also, these funds have tended to make the small individual investor more conservative in the sense that they have attracted his interest away from highly speculative commitments.

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FINANCING SMALL BUSINESS - Appendix I

130. Generally a worthwhile project requiring \$500,000 or more can be financed with a debt or equity issue. Small business requirements are therefore defined as being less than this amount.



1 131. The small ~~business~~ can sometimes raise funds
2 by selling shares or notes to friends and business
3 acquaintances of the entrepreneur. Occasionally, invest-
4 ment dealers will place an issue with a small group
5 of clients or with one or two investing institutions
6 out of the few willing to participate in private place-
7 ment. In a survey reported on by 103 investment dealers
8 there were 47 who had offered a total of 217 small
9 business issues in the past two years. Of this number only
10 18 were private placements.

11 132. The Industrial Development Bank has been
12 Canada's best answer to the problem of financing
13 small business. The I.D.B. reports having 1,364
14 loans totalling \$71.2 million for an average of \$52,000
15 per loan. Loans are only granted on the security of
16 fixed assets. In surveying the attitude toward the
17 I.D.B. the following criticisms were encountered:
18 that its services are too slow; costs too high; liens
19 on assets too tight; repayment requirements too heavy
20 and that there was a tendency to force small business
21 into fixed obligations. In spite of these criticisms
22 it appears to us that the I.D.B. is doing a good job.

23 133. The prime suppliers of short term loans
24 to small business are the chartered banks. Also,
25 under the Small Business Loans Act, the banks can advance
26 up to \$25,000 in certain small businesses grossing less
27 than \$250,000 per year. The Government guarantees lending
28 banks to the extent of 10 per cent of the aggregate
29 of such loans. Loans under this Act have not been as
30 numerous as was originally anticipated. It has been



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1 indicated that the Government might increase the maximum
2 to \$50,000 and include businesses grossing up to
3 \$750,000. This would be advantageous. However, the
4 Government should consider increasing its guarantee
5 to 25 per cent of the aggregate loans.

6 134. Public distribution of the securities of
7 small business is made difficult by the reluctance
8 of the chief lending institutions to participate
9 in small stock and bond issues. Thus, the underwriter
10 must rely on the retail buyer. The large investment
11 dealer cannot afford to handle small issues but if an
12 issue has sufficient merit an investment dealer can be
13 found to distribute it, if it is in excess of \$200,000.
14 Major problems which dealers experience in financing
15 small business are lack of depth and experience in
16 management; inability to withstand a recession;
17 reluctance of the principals to accept partners; an
18 insufficient amount of equity provided by the principals
19 and the lack of marketability of small issues.

20 135. Certain industrial commissions assist small
21 business through grants of land and communication of
22 taxes and some private corporations have been set up
23 to finance the small business. In the main, the latter
24 tend to require too large a share in the common stock.

25 136. In Britain the Industrial and Commercial
26 Finance Corporation plays a valuable role in financing
27 small business. This corporation is sponsored by a
28 group of banks. The shareholding banks provide all the
29 funds for its purposes. In the United States the Small
30 Business Administration has contributed importantly to



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1 financing of small business ventures. This
2 Administration licenses, supervises and helps to finance
3 investment companies which serve as sources of equity
4 and long-term loans to small business. About 425 of these
5 investment companies with capital amounting to \$ $\frac{1}{2}$
6 billion have been established. Subject to certain
7 limits they may borrow up to 50 per cent of their capital
8 from the Administration. Over 125 American banks are
9 stockholders of these investment companies. Consider-
10 ation should be given to establishing similar
11 legislation in Canada.

12 137. It is important to emphasize that the
13 largest pools of money in Canada, namely those of the
14 banks and the insurance companies, are at present
15 supplying no consequential amount of long-term funds
16 for small business. If ways and means could be found
17 to encourage these investing institutions to apply even
18 a fraction of 1 per cent of their portfolio investments
19 to the securities of small businesses, a major
20 contribution would result.

21
22 NON-RESIDENT INVESTMENT - Appendix M

23 138. Appendix M deals with certain aspects of
24 non-resident investment in Canadian debt securities.
25 Non-resident investment in equity securities is dealt
26 with in Appendix J.

27 139. Foreign investment in Canada rose from
28 \$7.1 billion in 1945 to \$20.6 billion in 1959. In 1959
29 U.S. investments in Canada totalled \$15.7 billion.
30 During the period 1946 to 1949, Canada was a net



financing of small business ventures. This Administration licenses, supervises and helps to finance investment companies which serve as sources of equity and long-term loans to small business. About 425 of these investment companies with capital amounting to \$1.5 billion have been established. Subject to certain limits they may borrow up to 50 per cent of their capital from the Administration. Over 125 American banks are stockholders of these investment companies. Consideration should be given to establishing similar legislation in Canada.

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During the period 1946 to 1949, Canada was a net



1 exporter of capital but her dependence on imported
2 capital increased during the 1950's and in 1959 over
3 29 per cent of gross capital formation was financed
4 through foreign sources.

5 140. Direct investment accounts for approximately
6 two-thirds of all foreign investment in Canada. In
7 recent years, the U.S. has been the primary source
8 of direct investment. Canadian tariff policy has
9 encouraged foreign companies to open branch plants in
10 Canada. The investment dealer has had little to do
11 with direct investments as they have been almost
12 entirely outside the realm of his operations.

13 141. In the area of portfolio investments however
14 the dealer has responded to the huge demands for capital
15 in Canada and sought out foreign markets for Canadian
16 securities. Foreigners have, in large part, financed
17 all the large pipelines, the development of the iron
18 mines in Quebec, the Kitimat aluminum project, and, in
19 a substantial part financed large hydro projects in
20 most of the provinces and a great many municipal and
21 provincial projects.

22 142. In the 1956 - 1960 period, external sales
23 of new issues of provincial, municipal and corporate
24 debt securities totalled over \$2.8 billion. The major
25 portion of these securities were payable in foreign
26 currencies. External payment bonds are legal for many
27 foreign investing institutions and were sold at yields
28 below those of comparable Canadian pay securities.
29 The latter are issued primarily for the Canadian
30 market and while purchased by foreigners they are not



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142. Provincial Securities

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The latter are issued primarily for the Canadian market and while purchased by foreigners they are not



1 nearly as acceptable to foreign institutions. The
2 main foreign purchases of Canadian debt securities
3 have been life insurance companies, pension funds,
4 savings banks and the like. Non-resident insurance
5 companies which write insurance in Canada buy
6 Canadian pay securities to cover their liabilities.
7 These purchases do not affect our balance of payments
8 position.

9 143. It is interesting to note that the greatest
10 flow of capital to Canada occurred when the dollar was
11 at a substantial premium. This suggests that the
12 exchange rate was a result rather than a cause of the
13 capital flow. However large capital inflows in 1950
14 and 1951 were undoubtedly related to the fact that
15 foreigners felt that the Canadian dollar was at an
16 unnaturally low level.

17 144. Since 1950, yields on Canadian bonds have
18 always been higher than those on comparable U.S. bonds.
19 The lower interest cost of financing through external
20 pay securities has appeared to be attractive to many
21 Canadian borrowers. Undoubtedly yields in Canada
22 during the 1950's were kept lower than they would have
23 been by virtue of the large volume of securities sold
24 in the U.S. Debt security sales were encouraged by
25 the absence of Canadian withholding taxes on external
26 payment bonds. Since late 1960 the Government has
27 actively discouraged sales of securities abroad by
28 asking provincial and municipal governments to finance
29 at home and by imposing withholding taxes which reduced
30 yields to certain foreign purchasers. This resulted



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1 in a substantial decline in the sales of debt
2 securities to foreign investors, and a rise in the
3 proportion of Canada's balance of payments deficit
4 being covered by direct investments.

5 145. A growing country like Canada may need to
6 import substantial amounts of foreign capital from time
7 to time to ensure a rate of growth consistent with
8 national objectives. It would seem desirable that
9 where foreign capital is required, it should be sought
10 in the form of debt rather than equity. In so far as
11 is possible, Canadians should be encouraged to
12 participate in the ownership of domestic enterprises.

13
14 TAXATION - Appendix N

15 146. In 1939, all levels of government in
16 Canada took approximately 20 per cent of the Gross
17 National Product. By 1960, this had increased to 28.7
18 per cent of a vastly increased Gross National Product.
19 With the background of rapidly increasing government
20 spending in mind, it appears essential that the tax
21 structure should be critically examined.

22 147. Growth of our economy depends on demand
23 for the goods and services we produce. Growth is
24 essential to the maintenance of a high level of
25 employment. Today the heavy tax loads and the methods
26 of applying them appear to have a profound effect on
27 economic growth. Under these conditions, it is desirable
28 that our whole tax system be re-assessed. At the
29 present time, Queen's University in co-operation with
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1 the Canadian Tax Foundation is carrying out a study
2 of the level and structure of taxation in Canada.

3 While broad, this study will not encompass all of the
4 areas which we believe should be examined.

5 148. The present tax system was formulated under
6 pre-war conditions. Since that time, the Canadian
7 economy has undergone substantial change. In addition
8 to the United States, new large economic blocks have
9 been formed which are influencing and will further
10 influence our international trading patterns. It is
11 probable that our tax system is quite unsuited to
12 current circumstances.

13 149. The prime factor which should be kept in
14 mind when considering the revision of the tax system
15 is simplicity. In Canada today, taxes are not only
16 high but also difficult to determine. Present patch
17 work results in considerable effort being utilized
18 in tax avoidance. Broadly speaking, the simpler
19 the tax system the easier it will be for business
20 to make decisions.

21 150. Another important goal in revising Canada's
22 tax system should be to achieve a more equitable
23 distribution of taxes - a distribution which
24 would provide more incentives and less discrimination.
25 We should strive for elimination of the various forms
26 of double taxation. Certain groups such as co-operatives
27 and credit unions should contribute their fair share
28 of the tax load. Particularly careful consideration
29 should be given to a reduction in the higher marginal
30 rates of personal taxation which would increase



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1 incentives. Is it right for an individual tax payer
2 to pay higher rates than the largest corporations?
3 151. The use of indirect taxation to broaden
4 the tax base should be carefully considered. In Canada
5 almost 86 per cent of tax payers pay less than the average
6 rate. If the revenues of government must be increased
7 substantially, a broader tax base will be necessary.
8 This could be achieved through indirect taxation.
9 Indeed, it might be desirable to implement a higher
10 sales tax in order that corporate income and personal
11 income taxes might be greatly reduced. In Canada at
12 present many individuals receive benefits but do not
13 pay their fair share of the costs. This also applies
14 to a number of corporate entities.
15 152. While taxation is punitive, it can be varied
16 in such a way as to direct and encourage economic
17 activity along desirable channels. Two important
18 channels for Canada are those that would lead to
19 increased exports and employment. An incentive of fairly
20 large proportions must be granted to ensure that movement
21 in the desired direction will occur. It might, for
22 example, be desirable to permit industry to charge
23 depreciation in excess of 100 per cent under certain
24 conditions.
25 153. In studying Canada's tax system, a full
26 examination should also be made of systems in other
27 countries, particularly those countries where production
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29 Consideration of the way these countries have orientated
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2 154. ~~These~~ Problems relating to distribution of corporate
3 surpluses might be solved in a better manner than at
4 present. Existing laws necessitate much wasteful
5 expenditure of time and energy in legal manoeuvres.
6 Consideration could be given to establishing a basic
7 flat tax at the corporate level on all distributions
8 to shareholders with such distributions then being
9 tax-free in the hands of the shareholders. The
10 establishment of the dividend tax credit was a
11 progressive move. Further steps toward the elimination
12 of double taxation should be considered. While the
13 dividend tax credit has been successful in encouraging
14 Canadians to invest in equities, it has not noticeably
15 induced corporations to finance through equity rather
16 than debt securities. Corporation tax levels are
17 apparently sufficiently high that they provide positive
18 preference for debt financing.

19 155. ~~Any~~ Any full study of the tax structure should
20 include a more precise definition of income with a
21 view to differentiating between income and capital
22 gains. For Canada a capital gains tax is neither
23 necessary nor desirable. Capital gains taxes can
24 cause severe market dislocations and the costs of their
25 calculation and collection are high.

26 156. The tax disadvantage experienced by Canadian
27 individuals in the development of natural resources
28 as compared with individuals in the United States
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1 development of natural resources. Absence of such a
2 privilege in Canada may have contributed significantly
3 to the high percentage of Canadian natural resources
4 which are foreign controlled.

5 157. A prime objective in planning the revision
6 of our tax system should be to provide a system which
7 will assist the orderly growth of the economy. The
8 government has been inclined to use increases in income
9 taxes as a means of controlling inflationary pressures
10 in boom periods. There has been no compensating
11 policy of reducing income taxes during recessions.
12 Canada needs to discover a positive approach to taxation
13 through which the tax structure will be more closely
14 linked to our long term economic and fiscal objectives.
15 This will necessitate a sweeping revision of the present
16 Income Tax Act. It is essential that a thoroughly
17 competent body study our tax structure and our needs
18 with great care. In the light of this study such a body
19 could suggest a new system or a general revision of the
20 old one which would be compatible with the requirements
21 of the new era in which we live. To achieve this end,
22 we recommend the establishment of a Select Committee
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APPENDIX TITLE

- A The Industry (Part 1) & the Association
(Part 2)
- B Finance Department and Federal &
Provincial Finance
- C Bank of Canada
- D Municipal Finance
- E Corporation Finance (Part 1) & Legislation
(Part 2)
- F Secondary Bond Market
- G Short Term Money Market
- H Chartered Banks and "Near Banks"
- I Retailing Bonds & Stocks; Risk Capital
- J Stock Business
- K Mutual Funds
- L Financing Small Business
- M Non-resident Investment
- N Taxation



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	Financing Small Business
N	Taxation



APPENDIX A

THE INDUSTRY AND THE ASSOCIATION

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APPENDIX A

ALISTRY AND THE ASSOCIATION

PART I THE INVESTMENT DEALERS' ASSOCIATION

Origins and Development

The Investment Business Today

Member Firms and Personnel

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Conclusion

Appendix

PART II The Investment Dealers' Association

History

Structure and Organization

(a) Constitution and By-laws

(b) Organization

(c) Comparison with United States and United Kingdom Organizations

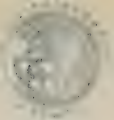
Functions

(1) Protection of the Investing Public

(a) Type of Business



1	(b) Minimum Capital Requirements	A.138
2	(ii) Mutual protection of Members	A.139
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PART I

THE INVESTMENT BUSINESS - AN OVERVIEW

Origins and Development

1. The roots of the investment business go back to the 1880's, when the first securities houses were founded. At that time most industrial and commercial businesses were small in size, their capital needs were modest and the use of the corporate form was not widespread. There were relatively few Canadians with surplus savings who were seeking investment opportunities and most of the long-term capital came from the London market. Canadian dealers established connections with English banking houses and acted as agents in arranging the sale in London of Canadian municipal and other securities.

2. By the turn of the century investment dealer operations had grown to include arranging capital issues for corporations engaged in transportation, public utilities and manufacturing. For example, in 1899 we find a dealer inviting subscriptions for \$300,000 of \$100 per value 7 per cent preferred shares of Dunlop Tire and Rubber Goods Co. Limited. This issue was well over-subscribed and allotments were made on the basis of 1 in 10.

3. In the early 1900's, as a result of continuing economic growth, more corporations sought "outside" capital and investment dealers underwrote and sold quite substantial issues. Thus in June 1911 we find a group of three dealers offering \$1,500,000 of 6 per cent First Mortgage Sinking Fund Bonds of Canadian



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1 Locomotive Company Limited. It would appear that these
2 bonds were still in primary distribution in late October,
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4 4. At that time costs of doing business were
5 low and spreads were wide by today's standards and the
6 sale of a new issue was a leisurely affair, usually
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8 legislation nor prospectus requirements. Sales effort
9 consisted of the preparation of a brief circular which
10 was mailed to a relatively short list of known investors.

11 5. When War broke out in 1914 more than
12 three-quarters of all new issues of bonds were still
13 being placed in London. Within a year this source of
14 funds had dried up and after a brief period of access to
15 the New York market, Canada was forced to turn to
16 domestic sources of funds to finance her War effort. In
17 1916, the 32 investment dealers then in business formed
18 themselves into what is now The Investment Dealers'
19 Association of Canada and set about organizing a Victory
20 Loan sales campaign which reached eventually every town
21 and village in the land.

22 6. The first domestic War Loan was offered
23 in 1915, was over-subscribed and was followed by
24 successful Loans in 1916, 1917, 1918 and 1919. In six
25 Loans over \$2.2 billion was raised from 2,845,171
26 subscribers -- an impressive sum for a country of
27 Canada's size -- and marked the beginning of a new
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29 7. In 1920 the Minister of Finance requested
30 investment dealers and banks to form a Marketing Committee

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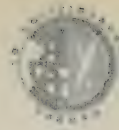


to stabilize the market for Victory Bonds. Heavy sales by Canadian holders of Victory Bonds and a fall in sterling exchange which triggered a return flow of Canadian securities from the United Kingdom, threatened to cause precipitous price declines. The Committee succeeded in maintaining orderly market conditions and achieving a redistribution of some \$150 million of "Vics".

8. The upsurge of industrial development in the decade following the First World War was facilitated by the presence in the country of thousands of new investors who extended their purchases to include new issues of bonds and shares arising from the growth of railway and transportation systems, hydro-electric power installations and the establishment and expansion of resource development and secondary manufacturing industries. This was a period of great activity for the securities business and over 80 new investment houses were founded between 1920 and 1929. Some idea of the increase in new issue financing during this period is given by the following table:

	<u>1920</u>	<u>1925</u>	<u>1929</u>
	(millions of dollars)		
Federal	} 126	} 319	139
Provincial			
Municipal	56	52	97
Corporate	46	126	298

9. This period saw the development of the syndicate system for underwriting and distributing new issues. As the size of individual underwritings grew, it became prudent for the investment dealer purchasing the



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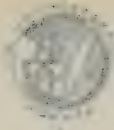
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1 securities -- sometimes known as "the house of issue" --
2 to organize a syndicate of dealers who would share the
3 liability by agreeing to underwrite part of the issue,
4 usually at a small increase or "step-up" from the
5 original purchase price. Today this syndicate is called
6 the "banking group". To be a banking group member a
7 dealer must have the financial strength to undertake the
8 liability. Larger issues require a greater selling
9 effort and, in due course, we find the banking group
10 inviting other dealers to join a "selling group," again
11 at a step-up from the banking group price. The selling
12 group dealers are each offered a participation or may
13 be invited to place an order with the manager of the
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15 limited to the actual amount of securities allotted to
16 him. Most new issues have been and are underwritten
17 in Montreal and Toronto but selling group members are
18 selected from various parts of the country in order to
19 secure the widest distribution possible.

20 10. The house of origin began to accept
21 increasing responsibility for co-ordinating the sale of
22 the new issue and for the maintenance of orderly marketing
23 conditions while the issue was being distributed. These
24 arrangements were not the invention of any one firm but
25 evolved out of the conditions under which the dealers
26 operated.

27 11. Subsequent to 1929 the investment business
28 passed through a period of trial and tribulation. As the
29 great depression settled upon the world, earnings and
30 tax collections dwindled and security prices declined



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1 disastrously. Many municipal and corporation issues
2 defaulted on interest payments and fear spread among
3 investors. Investment dealers suffered heavy losses
4 and many substantial firms hovered on the edge of
5 insolvency. The sharp decline in securities prices
6 which followed when Britain went off the gold standard
7 in 1931 impressed upon the dealer community the
8 importance of speeding distribution of new issues to
9 reduce the time during which a new issue liability was
10 carried. As the crisis passed, underwriting houses and
11 investing institutions worked away at problems involving
12 corporate reorganizations and plans for debt readjustment
13 of municipal and provincial issuers. Many municipal-
14 ities sought and obtained from investment houses which
15 specialized in municipal debentures, advice and
16 assistance with debt and financing problems. The
17 decline in volume of new issues in the early 1930's led
18 to greater emphasis upon activity in the secondary or
19 between-dealer market.

20 12. Increasingly vigorous competition for
21 what little business was available resulted in the dealer
22 becoming more competent in appraising the strong and weak
23 points of securities and more skilful in putting together
24 proposals for the exchange of securities owned for other
25 securities which offer the investor some advantage of
26 price, term, yield or other feature. A substantial
27 volume of business developed in the movement of Canadian
28 securities between Canada and foreign countries as
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30 their climb and taxation considerations offered dealers



definitely, many of the new issues were
definitely on interest payments and fear spread among
investors. The sharp decline in securities prices
which followed when Britain went off the gold standard
in 1931 impressed upon the dealer community the
importance of speeding distribution of new issues to
reduce the time during which a new issue liability was
carried. As the crisis passed, underwriting houses and
investing institutions worked away at problems involving
corporate reorganizations and plans for debt readjustment
of municipal and provincial issuers. Many municipal-
ities sought and obtained from investment houses which
specialized in municipal debentures, advice and
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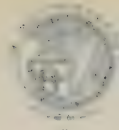


1 a new area where they could serve their clients and
2 develop new business.

3 13. Paralleling this growth in dealer "know-
4 how" came increasing discrimination on the part of
5 investors -- especially institutional investors who were
6 coping with securities which had failed to perform as
7 anticipated. This climate of difficult markets, more
8 selective buyers, lower volume of business and strenuous
9 competition between investment dealers was in marked
10 contrast to the buoyant, relatively unsophisticated
11 1920's when the dealer was principally concerned with
12 underwriting and distributing new issues and, in view
13 of the unbroken debt record of borrowers, had no reason
14 based on experience to build into security issues an
15 "extra" margin of safety against depressed economic
16 conditions.

17 14. In retrospect, it can be seen that the
18 1930's provided investment dealers, issuers and investors
19 with unforgettable lessons in the hard school of
20 experience -- lessons which were later reflected in
21 improved municipal financing standards and generally
22 better-designed municipal and corporate new issues.

23 15. During the years 1940-45 activity in the
24 securities business centred in the work of the National
25 War Finance Committee. Once again the Federal Government
26 called on dealer personnel to serve on national and
27 regional committees to spearhead the sales organizations
28 which blanketed the country. The magnitude of this
29 effort is indicated by the results: in two War Loans and
30 nine Victory Loans over 23 million subscriptions were



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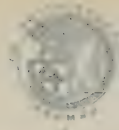
secured totalling some \$13.1 billions.

16. The investment industry began the post-war period with the conviction, based on the number of Canadians who had purchased Victory Bonds, that it was feasible to build a much larger securities business. During 1945-46 industry leaders, through the agency of The Investment Dealers' Association of Canada, initiated a long-range programme of action designed to raise minimum capital requirements of Member firms, ensure the maintenance of the highest ethical standards, develop employee training facilities and provide investment courses for the general public. The results of this major effort on which was expended thousands of man-hours, are given in part 2 of Appendix A.

17. The growth of the investment business in the post-war period exceeded all expectations. One example: in 1915 three dealers underwrote and sold over a period of some weeks \$1 million of Province of Ontario, 10-year 5's which were free of all provincial taxes, including succession duties. In 1955 a group of some 30 dealers and banks underwrote and distributed widely in one day \$100 million of Ontario Hydro 22-year 5's at par despite the prevailing high level of taxation on income.

The following table gives some idea of the volume of public new issues of bonds since 1946:

	New Issues (millions of dollars)			
	1946	1951	1956	1961
Federal	4,863	4,059	7,777	9,372
Provincial	115	379	557	998
Municipal	129	218	318	443
Corporate	584	453	860	568



16. The investment industry began the post-war period with the conviction, based on the number of Canadians who had purchased Victory Bonds, that it was possible to build a wide range of investment business.

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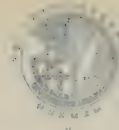
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	1946	1947	1948	1949
Federal	4,863	4,059	7,777	9,375
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1 The increase in volume, however, has been accompanied by
2 some new patterns due, among other factors, to the
3 following influences:

4 18. At the end of the War investors and
5 financial intermediaries were large holders of Government
6 of Canada Bonds. When it became apparent that expansion
7 rather than recession lay ahead, selling of Canada
8 obligations began as the need for liquidity increased
9 and the investment business entered upon a period --
10 still with us today -- of complex problems surrounding
11 the buying and marketing of Canada Bonds. These
12 problems involve, in addition to the management of the
13 national debt by the authorities, the use of the bond
14 market in the implementation of monetary policies, the
15 use of Federal deficit financing when slack exists in
16 the economy and a decreasing investor appetite for
17 long-term Government of Canada obligations. Demand-supply
18 factors are no longer the chief consideration of the
19 dealer in Canada obligations.

20 19. From 1950 to 1960 an up-swing took place
21 in investor demand for equities. This demand, which was
22 accentuated by the 20 per cent tax credit, stemmed from
23 two conflicting motivations -- a desire to share in
24 Canada's economic growth and also to acquire a hedge
25 against further decline in the purchasing power of our
26 dollar. An increasing proportion of the dealer's
27 earnings derived from stock business. New issues of
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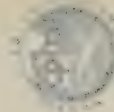
1 been accompanied by a growing investor preference for
2 fixed income securities which offer protection against
3 market fluctuations, e.g., Canada Savings Bonds and the
4 Parity Bonds issued by certain provinces.

5 20. By 1945 Bank of Canada had become the
6 dominant factor in the high grade bond market, both from
7 the standpoint of holdings of Canada bonds and of trading
8 activity. This made it imperative that the dealers
9 should understand central bank policy. Sometimes this
10 was difficult.

11 21. Since the introduction of the money market
12 in June, 1954, investment dealers have generated a large
13 volume of trading in short term securities and have shown
14 corporation treasurers, municipal officials and other
15 holders of short-term balances how to use these funds
16 more effectively. Today a varying, but substantial,
17 proportion of the industry's inventory is financed
18 outside the banking system.

19 22. Increased financial capacity and the
20 employment of more specially trained staff have enabled
21 dealer organizations to underwrite and distribute much
22 larger issues than in the pre-war period in spite of
23 keener competition which has narrowed profit margins both
24 in the primary and secondary markets. Costs of doing
25 business rose steadily during the 1950's and it has
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1 companies, pension funds, bond and stock pooled funds,
2 investment companies and so on) and a number of dealers
3 are specializing in transactions with such institutions.

4 24. Investment dealer facilities, including
5 branch offices in the United States, United Kingdom and
6 Europe, for the sale and purchase abroad of Canadian
7 securities increased during the 1950's and were a
8 significant factor in stimulating foreign interest in
9 Canada.

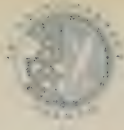
10 25. The history of the investment business to
11 date, covering periods of war and peace, prosperity and
12 recession, demonstrates its capacity to adapt itself to
13 varying conditions, including changing investor
14 preferences and fluctuating demands for capital.

15 THE INVESTMENT BUSINESS TODAY

16 26. Although influenced by practices and
17 institutions in the older London and New York markets,
18 the investment business in Canada is the result of a
19 gradual evolution to meet conditions in our own economy.
20 Here is a brief description of the business as it is
21 carried on today:

22 Member Firms and Personnel

23 27. As at December 31, 1961, the Investment
24 Dealers' Association of Canada had 189 Members,
25 employing 9,329 persons including shareholders and
26 directors (See Exhibit A). (The Membership as this is
27 written -- April 1st, 1962 -- stands at 190). A similar
28 survey taken in August 1958 showed 196 Member firms,
29 employing 8,589 persons (see Exhibit B). These two
30 surveys reveal a reduction in Membership of 7 and an



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1 increase in the number of personnel employed of some
2 8 per cent.

3 28. The number of office workers required to
4 support one salesman or trader has been rising due to the
5 employment of more specialists, such as analysts,
6 engineers, etc., and the increased paper work involved
7 in producing the growing number of reports required for
8 governments and for management. Most of the young men
9 being recruited for sales, underwriting, trading, and
10 research work are university trained. "A CAREER IN
11 FINANCE" issued by the Association in May, 1962, outlines
12 the approach to in-service training of employees used
13 by many firms. A copy of this booklet is attached
14 hereto.

15 29. Membership in the Association has fallen
16 from its peak of 206 in 1955 to its present (April 1962)
17 level of 190. During this period 47 members resigned
18 and 31 new members were accepted. Reasons for
19 resignation are given in Exhibit C.

20 30. Exhibit A shows that in December 1961,
21 110 Members had staff of less than 25 and the 1958 Survey
22 suggests that over 60 of these employ 10 persons or less.
23 In this size of business a few senior partners possess
24 the capital, the clientele and the expertise which makes
25 the business possible. This type of enterprise has
26 a very "personal" quality and is more likely than the
27 larger dealer to encounter problems of continuity of
28 management, including the training and retention of able
29 young men to carry on the business.

30 31. Exhibit A reveals the essentially small-
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Page 10

CONFIDENTIAL

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31. Exhibit A reveals the essentially stable-



1 character of the investment dealing business and the
2 substantial proportion (14.5%) of personnel who are
3 partners or shareholders of Member firms or corporations.
4 The Association has deliberately kept its minimum capital
5 requirement (\$25,000) low to encourage applications from
6 small investment houses which can meet our standards as
7 to type of business, character and competence. The
8 owners of investment houses are active in the business
9 and there is no absentee ownership except for eleven firms
10 controlled in the United States and most of the latter
11 have one or more resident directors in charge of
12 Canadian operations.

13 32. While the investment business is
14 concentrated in the metropolitan areas of Toronto and
15 Montreal, it is well-diversified geographically as
16 revealed by the following table:

17	<u>Area Served</u>	<u>Number of Members</u>
18	1 Province	144
19	2 Provinces	25
20	3 " "	4
21	4 " "	4
22	5 " "	4
23	6 " "	3
24	7 " "	3
25	9 " "	<u>2</u> <u>189</u>
26	Number of Members with foreign 27 head offices	<u>10</u>
28	Number of Members with branches 29 abroad	<u>30</u>



1931
A-1

Canadian Investment Association
1931

REPORT OF THE CANADIAN INVESTMENT ASSOCIATION FOR 1931

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Number of Members with foreign head offices 10

Number of Members with branches abroad 30



The Internal Organization of an Investment House

33. The organization chart given in Exhibit D provides some idea of the internal set-up of the larger investment house. The officers and directors of a typical house of this size include a Chairman, President, 3 - 6 Vice-Presidents (one of whom may be Executive Vice-President) and from 9 - 12 other Directors. Most of these Directors are located in the head office, but some may be in charge of principal branches in other parts of Canada and abroad. Incorporation as a private company is usual with the holding of shares being limited to officers, directors and employees. The total number of shareholders is less than 50 with principal shareholders (5 per cent or over) somewhere in the region of 6 - 10, all of whom will be officers or senior directors. Retirement in the larger houses is usually mandatory at 65 and the retirement of principal shareholders is effected by gradual disposal of their shares starting when the shareholder reaches a stipulated age and continuing until retirement age, by which time the shareholder will have disposed of his entire holding.

34. Since the large investment house has few officers compared to its opposite number in banking and insurance, lines of authority are relatively flexible and frequently a director will fulfill more than one responsibility, e.g., Vice-President in charge of Sales and Syndicating. As a result of the need for flexibility, there is a wide diversity of practice in the allocation of duties among senior officials and lines of responsibility are frequently blurred. Large



1 investment houses are very individualistic in the way
2 in which management functions are divided, e.g., in some
3 firms the Chairman of the Board plays a dominant role in
4 the management of the firm, in others the post is a
5 recognition of distinguished service and the Chairman is
6 regarded as an elder statesman and counsellor. As we
7 move from the larger investment firm to the medium size
8 and smaller firm we find the senior officials in closer
9 contact with the overall operation of the firm. Thus
10 you may find in the small house that the Secretary-
11 Treasurer is also a Director and his principal occupation
12 may be sales. In the small firm the senior officials
13 are responsible both for policy and direction and active
14 in the day-to-day operation of all phases of the business.

15 35. Policy establishment and decision making
16 rest with the Chairman....President....Vice-President
17 group, i.e., the senior partners. Underwriting
18 negotiations are usually handled by one of this group
19 and when the informal agreement has been signed other
20 specialists take over. Inventory is the responsibility
21 of a Vice-President usually with limits below which he
22 need not consult his partners. The formulation of
23 investment recommendations to clients is often delegated
24 to a specialist who has ready access to senior officers
25 or may report to a special committee of the Board.
26 Employment of trainees for sales, underwriting, trading
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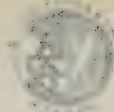


1 concerned with all phases of management.

2 36. Since the investment dealer handles daily
3 cheques and frequently-negotiable securities running into
4 large sums, the industry has developed, over the years,
5 routines of control and checking to protect these assets
6 from loss, theft or conversion. The Association
7 requires Member firms to carry certain minimum fidelity
8 insurance coverage and the firm must segregate and
9 earmark clients' free securities. Each Member firm is
10 required to select its auditor from a panel approved by
11 the Association's District Auditor. Association By-
12 laws set forth the requirements for the submission of
13 financial statements to the Association's Auditors and
14 any Member which gives concern to the District Auditors
15 are immediately reported to a confidential Audit
16 Committee which has the power to take swift and effective
17 action in correcting the situation. Some larger houses
18 also maintain internal audit facilities which supplement
19 those of the Association. All Member firms select staff
20 carefully and endeavour to the best of the facilities at
21 their disposal to train staff to carry out their duties
22 in an honest and competent manner.

23 Types of Houses

24 37. The term "investment dealer" embraces a
25 variety of types of securities business, reflecting in
26 turn the many types of clientele which must be served.
27 It is not possible to list under definite headings the
28 various classifications of dealers as there is always an
29 overlapping as well as a variation in the business
30 transacted by various types. However, in general terms



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investment dealers may be divided into three groups:

The Integrated Houses which originate,

underwrite and distribute government
and corporate securities; manage banking
and selling groups and participate in
other dealers' banking and selling
groups; maintain underwriting, sales,
trading, portfolio management,
statistical, research, accounting and
delivery departments and carry on a
stock brokerage business or operate
an affiliate brokerage firm which is a
Member of one or more stock exchanges.

Integrated investment houses may be
national in scope or operate within a
province.

Distributing Houses which do not customarily

originate industrial issues, but may
purchase municipal issues for distribution
on their own account; occasionally may
be members of a banking group and
typically participate in selling groups;
vary from small operations with a staff
of four or five persons to larger firms
with substantially the same facilities,
aside from underwriting, as the integrated
investment houses.

Specialty Houses: in this category are

included those firms which concentrate on
a particular phase of the investment



1 business. Examples: dealers who
2 specialize in trading in outstanding
3 bond issues; dealers who restrict their
4 trading to stocks which are not listed
5 on the stock exchange; dealers who
6 specialize in municipal, school and
7 religious issues; dealers whose
8 principal business is that of a stock-
9 broker, but do operate a bond department
10 including the services of a bond trader.

11 Principal Functions

12 38. The work of the investment dealer can be
13 described under three headings: (1) underwriting and
14 primary distribution; (2) trading and secondary markets;
15 (3) informational, advisory and investment management
16 services.

17 Underwriting

18 39. The problem before a would-be issuer of
19 securities whether a government or a corporation is how
20 and on what terms can the capital be obtained. Since
21 there are always a number of approaches to a financing
22 problem one of the principal functions of the dealer is
23 to outline the alternatives and recommend what he
24 considers to be the best one in the current circumstances.

25 40. The principal types of financing involving
26 the use of the services of an investment dealer are:

27 (a) The purchase of all or part of an
28 issue at public tender -- frequently
29 used with provincial and municipal
30 securities. The dealer estimates

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there are always a number of approaches to a financing
problem one of the principal functions of the dealer is
to outline the alternatives and recommend what he
considers to be the best one in the current circumstances.
40. The principal types of financing involving

the use of the services of an investment dealer are:

- (a) The purchase of all or part of an
issue at public tender -- frequently
used with municipal and industrial



1 the yield at which the issue can
2 be sold, adds his anticipated gross
3 profit and calculates his bid.

4 (b) A negotiated, underwritten public
5 offering where the issuer and
6 dealer arrive by mutual agreement
7 at the type and terms of the
8 security to be purchased by the
9 dealer and sold to the public.

10 (c) A negotiated, underwritten stock
11 offering confined to shareholders
12 with the dealer agreeing to purchase
13 any of the new securities not taken
14 up by the shareholders.

15 (d) An "option" offering of an issue by
16 a dealer who acts as an agent.

17 (e) A "private placement" where the
18 investment dealer acts as the agent
19 of the issuer and negotiates the sale
20 to one or a few buyers, usually
21 investing institutions.

22 41. Whichever method is used, the dealer is
23 frequently called upon to accept two responsibilities:
24 obtain the funds on terms suitable for the issuer and
25 competitive with other issues in the market and, also,
26 ensure that the security is of sufficiently high quality
27 to warrant its offering to his clients.

28 Government of Canada Market Issues

29 42. When a new loan has been approved by the
30 Federal Government, the responsibility for effecting the



1 actual distribution is assumed by Bank of Canada. Over
2 the years the Bank has evolved more or less standard
3 procedures for bringing Government of Canada direct and
4 guaranteed loans to the market. These procedures are
5 subject to variation as market conditions change and as
6 new techniques are tested and do not apply to the sale
7 of Treasury Bills or special offerings such as the 1958
8 Conversion Loan. The Bank maintains a list of
9 investment dealers and banks which are eligible to take
10 part in the primary distribution of new Canada issues.
11 This list is, in effect, a large selling group. Since
12 1961 the financial community has been given a few days'
13 advance notice of the Government's intention to come to
14 market on a specified date. On the morning of that
15 day each primary distributor receives an "offering wire"
16 from Bank of Canada informing him of the details of the
17 loan, including the amount offered, price, coupon,
18 yield, term, method of offering, commission, deliveries,
19 payment, sub-agents and reports to be made to the Bank
20 and so on. Investment dealers immediately get to work
21 on the new issue and despatch subscription telegrams to
22 the Bank as soon as a decision can be taken. In some
23 issues the Bank offers each primary distributor a firm
24 allotment which is usually accepted in full. Primary
25 distributors are also permitted to apply for additional
26 bonds, sometimes without limit and sometimes to a
27 maximum which is related to the original allotment.
28 On other issues primary distributors must apply for
29 bonds, calculating how well the loan will be received
30 before entering their application by wire. Some loans

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1 are heavily over-subscribed and the primary distributor
2 may only receive a pro-rata allotment of his subscription.

3 43. On one occasion Bank of Canada, after
4 making allotments of firm bonds, invited primary dis-
5 tributors to tender for additional bonds. In recent
6 months the Bank has been effecting exchanges of
7 securities with the Government, which exchanges partake
8 of the nature of an advance refunding. In such cases
9 the Bank announced that it was open for bids or exchange
10 offers for the issue being made available and apparently
11 accepted or rejected bids and offers on the basis of
12 their individual appeal. Another technique used by
13 the Bank recently is the reselling of new issue bonds
14 which have been acquired directly from the Government,
15 a procedure which to some extent resembles a "tap"
16 loan. The Federal Government has made extensive use
17 of short-term issues during the past two years. As a
18 rule two maturities are offered at a specified price
19 less a concession to primary distributors who subscribe
20 in accordance with the extent of their orders and, in
21 due course, receive confirmation of their allotments.

22 PROVINCIAL NEW ISSUES

23 44. New issues of provincial governments are
24 generally sold by private negotiation or by tender. For
25 smaller issues tenders are sometimes invited from two or
26 more syndicates of investment dealers. In 1961, for
27 example, three groups of dealers tendered for a \$7.5
28 million, Province of New Brunswick issue. Large
29 provincial borrowings, in order to obtain the best results
30 from an orderly marketing, are often sold through



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1 negotiation to a large syndicate of dealers. Over a
2 long period the Ontario Government and the Hydro Electric
3 Power Commission of Ontario have used this method of
4 marketing. More recently the Provinces of Quebec,
5 Manitoba and Saskatchewan have adopted this procedure
6 of negotiating with large syndicates in order to achieve
7 market stability for their issues.

8 45. Provincial requirements for borrowed funds
9 have increased to the point where some provinces have
10 been casting about for new methods of raising capital.
11 A recent innovation has been the issuance by the Provinces
12 of British Columbia, Saskatchewan and Manitoba of Parity
13 Bonds, either direct obligations or guaranteed, cashable
14 at par and accrued interest at specified times each year.
15 A substantial proportion of these bonds were sold by
16 investment dealers on an agency basis and over \$300
17 million have been raised through this method of marketing.
18 Five provinces are issuers of short-term securities which
19 are "rolled over" as they mature.

20 46. The syndicate which buys the issue is
21 known as the "purchase group". Occasionally the purchase
22 group will invite other dealers to join, at a step-up,
23 in the formation of a banking group to share the
24 liability and in larger issues a selling group is usually
25 formed.

26 MUNICIPAL NEW ISSUES

27 47. Most new issues of municipal debentures
28 because of their generally smaller dollar size as
29 compared with provincial issues are sold through sealed
30 bids although many large issues and some smaller ones



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1 are sold by private negotiation. The cities of
2 Ottawa and Regina, for instance, after using both methods,
3 currently favour the negotiated sale as the more
4 effective for a city which faces a heavy borrowing
5 programme and thus a recurring need to come to market.
6 A syndicate of dealers which knows in advance that it
7 will have more of that municipality's debentures to sell
8 maintains a continuing interest in the outstanding
9 securities of the municipality and can prepare a good
10 reception for each new issue.

11 48. The procedure for selling new municipal
12 debentures by the auction method is more or less
13 standard in all provinces. After the necessary legal
14 requirements have been met, a call for tenders is
15 advertised in the Provincial Gazette and/or the daily
16 press in financial centres and a selected list of
17 dealers is circularized. Syndicate managers advise
18 their partners of the forthcoming issue. A meeting is
19 held at which the municipality's statistical record is
20 studied and a representative of the syndicate may visit
21 the municipality for firsthand talks with civic officials
22 and a personal inspection of the community. The
23 saleability of the new debentures is appraised and a bid
24 mutually agreed upon. The bid contemplates a profit
25 to the syndicate adequate to provide for expenses and
26 a risk factor but at the same time the bid has to be
27 pitched high enough to make it competitive.

28 49. After the bids are open, and without
29 reference to the issuer, the winning syndicate promptly
30 decides among themselves the method of sale and the



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49. After the bids are open, and without



1 amount of any concessions or allowances and the formal
2 offering of the securities is made to institutional and
3 other investors. The syndicate may consider it
4 unlikely that they will be able to dispose of the whole
5 of the issue as quickly as desirable or may wish wider
6 geographical distribution than obtainable from syndicate
7 members and decide to form a selling group. The size
8 and make-up of the selling group vary with the issue.
9 In joining a selling group a dealer agrees to abide by
10 the conditions of the offering and can request securities
11 at a discount from the public offering price, and he also
12 agrees to maintain the public offering price set by the
13 syndicate until the issue is sold or until released from
14 the agreement by the manager and to report daily to the
15 manager any unsold balances. Attached to the selling
16 group letter is a list of investing institutions which
17 are "exempt" from the general offering by selling group
18 members. These exempt institutions are contacted by
19 the syndicate members in a manner to avoid duplication
20 of coverage and profits from sales to exempt institutions
21 are for the account of the syndicate and confirmed by the
22 syndicate manager. Where an issue is over-subscribed,
23 the books are promptly closed, allotments made on orders
24 received and confirmations sent out to buyers.

25 50. The liability of each selling group member
26 is limited to the amount of the new issue which he has
27 requested to purchase. Syndicate members operate on a
28 larger spread but must pay syndicate expenses which
29 include concessions to selling group members, legal
30 expenses, cost of printing circulars, etc. and since they

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1 own the debentures are exposed to risk of loss while
2 distribution is underway.

3 MONEY MARKET NEW ISSUES

4 51. Money market securities include Government
5 of Canada treasury bills, Government of Canada bonds and
6 guaranteed bonds with an unexpired term of three years
7 or less to maturity (or to the earliest call date, where
8 a transaction is completed at a premium). Provincial
9 government treasury bills, treasury bills issued by
10 several large municipalities, finance company paper and
11 prime commercial paper are generally classed as being
12 in the money market but are not acceptable for rediscount
13 purposes at the central bank nor eligible for day-to-day
14 loans at the chartered banks.

15 52. Fourteen investment dealers, active in
16 the money market, and the chartered banks, tender each
17 Thursday for Government of Canada treasury bills.
18 Normally some of these bills are bought against orders
19 and the balance offered to investors and the chartered
20 banks. Provincial and municipal treasury bills and
21 short term coupon notes are purchased both at tender and
22 by negotiation and are sold to investors who have
23 temporary surplus idle cash. In the purchase of prime
24 commercial paper the dealer usually acts as an agent
25 receiving a nominal commission. Transactions in the
26 money market are characterized by large size and a very
27 small margin of profit.

28 CORPORATE NEW ISSUES

29 53. Corporation issues generally arise out of
30 direct and private negotiations between an underwriting

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1 house and the company. An historical relationship
2 grows up between the dealer and the company, with the
3 dealer having first refusal of any new financing. Among
4 the advantages to a company of such a fiscal agency is
5 the continuing interest of the dealer in the company's
6 financial affairs, continued sponsorship of its securities
7 in the market and the reduction to a minimum of the
8 number of persons with access to company confidential
9 information.

10 54. The underwriter preparing an issue for a
11 corporation which is coming to market for the first time,
12 makes a thorough investigation of its financial condition,
13 calibre and continuity of management and future prospects,
14 employing for this purpose such experts as engineers,
15 accountants and management consultants. Negotiations,
16 not infrequently run on for months before the decision is
17 taken to "come to the market". This trend to a more
18 thorough appraisal is due to the accumulating experience
19 of the underwriting house and is re-enforced by the
20 requirements of professional investors and "full
21 disclosure" securities acts. During the post-war period
22 our underwriting houses have faced and successfully solved
23 many intricate problems of corporation finance. The
24 pool of skill which exists among Canadian underwriting
25 houses is now very considerable and compares favourably
26 with that in the United Kingdom and United States.

27 55. In going to the public market a corporation
28 has a great number of vehicles available to it, including
29 common and preferred shares, bonds, debentures,
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1 variety of types of sinking funds, serial bonds and
2 term and coupon arrangements, plus a wide range of
3 covenants. The instrument created must be given
4 careful consideration in relation to the capital structure
5 of the company and the current preferences of the market.
6 It is within this milieu of alternative choices that the
7 investment dealer demonstrates his skill and resource-
8 fulness.

9 56. Once the decision to underwrite is made
10 the representatives of the underwriter and the officers
11 of the issuing corporation prepare and sign an informal
12 agreement covering the significant features of the
13 issue.

14 57. The question of the offering price and the
15 underwriting compensation are not finally decided until
16 just before the offering. The syndicate manager must
17 correlate all known factors in arriving at a decision,
18 carefully sounding out the probable reception for the
19 issue through talking with his own sales organization
20 and with his banking group associates. He then presents
21 to the financial officers of the issuing corporation
22 his conclusion as to offering price and underwriting
23 compensation. The matter is discussed freely and if no
24 real differences of opinion develop the terms are
25 presented to the Board of Directors and the arrangement
26 approved. The pricing of the securities is vital -- if
27 the manager prices the issue too cheaply he is subject to
28 criticism from the Company when the price rises sharply
29 in the after market. Should he price them too high the
30 banking group will be left with unsold balances on their

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1 hands and the issuing company will be critical of the
2 poor reception given its securities.

3 58. When the approval to issue has been given
4 by the Board of Directors, speed becomes a major
5 consideration and the issuer, the underwriter, counsel
6 for the issuer, counsel for the underwriter, the issuer's
7 auditors, the selected trust company, the printer of the
8 prospectus and the bank note company work together with
9 the goal in mind of producing the following documents:
10 the prospectus, the purchase agreement, syndicate letters,
11 the trust deed or indenture and the debenture certificate.

12 59. When the prospectus has been approved by
13 all concerned, it is signed by the directors of the
14 company and the underwriters and filed with the
15 appropriate government authorities, including the
16 securities commissions of those provinces in which the
17 underwriter intends to distribute the issue. At the
18 same time, the underwriter is drafting the purchase
19 agreement and, if there is to be a banking group, inviting
20 other houses to join the syndicate. The principal
21 factors governing the selection of dealers to be invited
22 to join the banking group are the issuing company's
23 preference, if any; distributing ability; geographical
24 location of offices; reciprocal business. The banking
25 group agreement which is signed by all participants
26 states the terms, including the price at which the
27 securities are to be sold, under which the distribution
28 is to be effected. Where the syndicate manager deems
29 it advisable a selling group is formed.

30 60. During the period when selling group terms



Department of the Interior
Bureau of Land Management

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it advisable a selling group is formed.
60. During the period when selling group terms



1 are in force the manager may move securities from
2 dealers who are experiencing a slow sale to those who need
3 more to fill orders. The duration of syndicate restrict-
4 ions in the past few years became shorter than previously
5 and it is not uncommon to find a syndicate with a life
6 of less than seven days although in a slow moving issue
7 you may find the restrictions in effect from the time of
8 the official offering to delivery date. When
9 distribution of the issue has been completed, the selling
10 and banking groups are terminated and each firm's share
11 of the profits after expenses is allotted pro rata.

12 61. Despite the best efforts of banking and
13 selling group dealers to place securities with investors
14 who will hold them, a certain amount of selling always
15 occurs before delivery date. Some of this stems from
16 speculators who had hoped to make a quick "turn" and some
17 from investors who intended to buy and hold, but due to
18 unforeseen circumstances must sell. To take care of
19 this inevitable selling the syndicate manager may "go
20 short" by an amount which he judges will mop up the return
21 flow of securities. The size of the short position is a
22 fine calculation to be made by an experienced syndicate
23 manager since an excessive short position can lead to
24 serious losses. When the issue is completely distributed,
25 all dealers who participated in the distribution, and
26 especially the syndicate manager, stand ready to provide
27 a secondary market in the issue.

28 62. Syndicate Managers accept responsibility for
29 the continuing "good health" of securities which they have
30 helped create and distribute. Should a company which has



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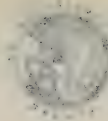
1 sold its securities to the public through investment
2 dealers develop financial difficulties, the underwriting
3 house will work with the company to solve the problem.

4 TRADING AND SECONDARY MARKETS

5 63. The second major function performed by the
6 investment dealer is trading in the secondary market and
7 the maintenance of an inventory of securities which makes
8 it possible to conduct an orderly market. The two
9 principal functions of the secondary market are: (a) to
10 bring buyers and sellers together and (b) to smooth the
11 course of the market by offsetting temporary variations in
12 the demand for and the supply of securities.

13 64. Secondary market transactions make possible
14 the change in ownership of securities, thus facilitating
15 primary distribution, and establish value levels for
16 outstanding securities. The secondary market consists of
17 two segments: (a) the organized stock exchanges and (b)
18 the street (also called over-the-counter, between-dealer
19 or unlisted) market. The street market includes all
20 fixed income securities and stocks not listed on stock
21 exchanges. At times, and under certain circumstances,
22 shares listed on a stock exchange may trade between
23 dealers who are not members of the exchange.

24 65. Here is how the street market operates.
25 Prices on the street market are generally determined by
26 negotiation between buyers and sellers although where
27 there is a series of bids or offers made in the process
28 of reaching agreement there is a degree of auction
29 present. There are approximately 200 dealers and a much
30 smaller number of banks and trust companies active in the



TRADING AND SECONDARY MARKETS

63. The second major function performed by the reverse dealer is listing in the secondary market and the maintenance of an inventory of securities which makes it possible to conduct an orderly market. The two principal functions of the secondary market are: (a) to bring buyers and sellers together and (b) to smooth the course of the market by offsetting temporary variations in the demand for and the supply of securities.

64. Secondary market variations are brought about by the change in ownership of securities, thus facilitating primary distribution, and establish value levels for outstanding securities. The primary market consists of two segments: (a) the organized stock exchanges and (b) the over-the-counter market. The stock market includes all fixed income securities and stocks not listed on stock exchanges. At times, and under certain circumstances, shares listed on a stock exchange may trade between dealers who are not members of the exchange.

65. Here is how the street market operates. Prices on the street market are generally determined by negotiation between buyers and sellers although there is a series of bids or offers made in the process of reaching agreement there is a degree of auction present. There are approximately 200 dealers and a much smaller number of banks and trust companies active in the



1 street market, which is principally located in Toronto
2 and Montreal. Dealers active in this market have up to
3 60 direct lines to other dealers, and to an occasional
4 bank, trust company or large institutional client. It
5 is this network of dealers and institutions connected by
6 telephone, teletype and telex which constitutes the
7 market.

8 66. Trading in the street market is carried on
9 by "traders". In the larger investment house the work
10 is divided among several traders with one handling money
11 market issues, another long Canada's and provincials,
12 another corporates and so on.

13 67. The sales and trading departments are
14 closely related, with the salesmen asking for quotations
15 for securities which clients wish to buy or sell and
16 traders providing salesmen with this information as
17 well as quotations on securities owned by the firm or
18 available on the street.

19 68. Speed is an important factor in a success-
20 ful trading operation and salesmen and traders are
21 positioned close together so that they can inter-
22 communicate quickly. This process is sometimes assisted
23 by a quotation board which immediately reflects all price
24 changes.

25 69. The Bank of Canada is a major factor in the
26 "street" market and traders in Toronto and Montreal keep
27 in close touch with Bank of Canada representatives in
28 these cities. The Bank does not call a market but
29 "responds" only to firm bids and offerings, hence dealers
30 are continually phoning the bank to test the market by



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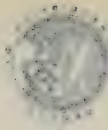


1 offering or bidding for blocks of Canada bonds.

2 70. Market information on price, volume, bids
3 and offers is obtained mostly by word-of-mouth by traders
4 talking to each other, but printed information is also
5 provided by some 25 dealers who issue daily, weekly or
6 monthly quotation sheets, and by the bond quotations which
7 are disseminated by the Association to some twenty dailies
8 and two financial weeklies. The Association's quotes,
9 since they are national, are slightly wider than most
10 dealer markets in retail size.

11 71. In order to have an effective secondary mar-
12 ket there must be a number of dealers who are prepared to
13 take securities into position. A security acquired and
14 held is part of the firm's long position. Inventory may
15 be acquired as a result of a slow-moving new issue which
16 will be gradually disposed of over a period of time, as
17 the result of a conviction that a security represents good
18 value and is a desirable merchandise to offer for sale to
19 clients or as a service to clients who wish to dispose of
20 securities. Size of the inventory carried is directly
21 related to the dealer's capital because of the
22 Association's minimum capital regulations which require
23 the margining of inventory held and also because of the
24 need of the dealer to maintain reserves for possible
25 future commitments. A "short position" arises when a deal-
26 er sells a security before he owns it. This may occur in
27 anticipation of price declines, in connection with a new
28 issue as previously described, or because the firm is an
29 active trading house striving to give quick service to a
30 client who wishes to buy.

72. With the growth in importance of



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70. Market information on price, volume, bids

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1 institutional investors, the demand for single executions
2 of large size is increasing. Many investing institutions
3 are active traders, exchanging holdings for new issues
4 and moving from one security to another as proposals are
5 "put up" to them by dealers or developed by the officers
6 responsible for managing the portfolio. Where a stock
7 is listed on a stock exchange, permission must be obtained
8 to execute an off-the-board sale. The exchanges permit
9 off-the-board "secondaries" over a stated minimum dollar
10 value because such transactions are beyond the capacity
11 of an auction market to process without disrupting prices.

12 73. The Investment Dealers' Association assumes
13 responsibility for the supervision of the street market,
14 assisted by the Bond Traders Associations of Toronto and
15 Montreal who provide what day-to-day overseeing is
16 required. Trading Regulations (see Exhibit F) cover
17 such points as good delivery, regular delivery, accrued
18 interest, buy-ins and control of employee trading.

19 OTHER INVESTMENT DEALER FUNCTIONS

20 74. Investment dealers provide services
21 ancillary to their principal function of dealing in
22 securities. These include provision of factual
23 information regarding securities and security issuers,
24 advice on investment problems and investment management
25 services.

26 75. Dealers provide their clients and
27 prospective clients with a continuous flow of information
28 concerning securities, including lists of offerings,
29 market commentaries, quotations, dividends, taxes and
30 called bonds.

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2 of large size is increasing. Many investing institutions
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19 Investment Dealers' Association

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25 75. Dealers provide their clients and
26 prospective clients with a continuous flow of information
27 concerning securities, including lists of offerings,
28 market commentaries, prospectuses, dividends, taxes and



1 76. On request investment dealers also provide
2 advice on specific investment matters including the
3 review of lists of securities and the making of specific
4 recommendations to buy, sell or hold. The quality of
5 this service is related to the firm's research and
6 statistical facilities. 78 of 177 Members reporting
7 state that they maintain a statistical and research
8 department staffed by at least one full-time specialist.
9 127 Members of 177 reporting advise that they provide
10 portfolio management services to clients. Typically,
11 these are not discretionary accounts, the client being
12 consulted prior to each change in the portfolio. Some
13 dealers impose an annual fee of $1/2 - 3/4$ per cent of
14 the value of the portfolio, which fee may be reduced by
15 the total of profits and commissions arising from
16 transactions effected for the account. Usually,
17 however, no charge is made for this service, the dealer's
18 compensation deriving from profits and commissions on
19 transactions made for the client. At least 14 dealers
20 operate investment companies, chiefly invested in
21 equities, whose shares are offered to the general public.
22 Some four dealers maintain pooled funds, participations
23 in which are available only to clients of the dealer
24 concerned. These pooled funds are designed to offer
25 small clients the advantages of diversification and
26 professional management in the same fashion as a mutual
27 fund.

28 77. Senior dealer personnel are from time to
29 time called upon to give expert testimony at rate hearings
30 and valuation cases and frequently serve on boards of

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time called upon to give advice to clients on matters of

and valuation cases and frequently serve on boards of



1 companies whose securities their firms have distributed.

2 CONCLUSION

3 78. The investment business because of its
4 complex character, its need to adapt continuously to
5 changing conditions, its confidential nature, the
6 essentiality of high ethical standards and the substantial
7 sums involved even in run-of-the-mill transactions is a
8 profession as well as a business. It is characterized
9 by narrow gross profit margins and the necessity for
10 developing volume if a house is to grow. In contrast
11 with the financial institutions with which they have
12 common boundaries, investment dealer organizations are
13 small and characterized by a high degree of independence
14 and individuality, in which pattern the views and
15 convictions of senior dealers are predominant.

16 79. Investment dealers -- individually and
17 through their Association -- have made a consistent effort
18 during the post-war period (tempered always by the need
19 and desire to consult in a democratic manner with nearly
20 200 Member firms and corporations) to raise standards of
21 financial capacity, competence and ethical practice. Mr.
22 J.E. Coyne, then Governor of Bank of Canada, in a public
23 address made on December 14, 1959, stated:

24 "....we also have in Canada a well
25 developed nation-wide capital market,
26 particularly in respect of the
27 distribution of securities issued
28 by governments, local authorities and
29 business corporations. This is
30 primarily the field of activity of



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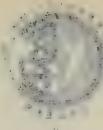
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1 investment dealers. I think there
2 is little doubt that the financial
3 machinery existing in Canada for
4 the placing of new issues of
5 securities on the market is the
6 equal of that of any country in the
7 world and, in proportion to our size,
8 it probably arranges, year in and year
9 out, for the provision of a greater
10 quantity of new capital to those
11 requiring it than is the case in any
12 other country in the world. The
13 results achieved are a reflection of
14 the industry and enterprise and broad
15 national outlook of our investment
16 dealers...."

17
18 - End -
19
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- End -



PART 1 - EXHIBIT "A"

PERSONNEL DATA

Notes: (1) This summary shows the total number of full-time staff employed by Members as at December 31, 1961.
(2) Members incorporated in, or with principal office in Canada, included entire staff, Members incorporated, or with principal office outside of Canada, included only staff employed in Canada.
(3) Summary includes only personnel engaged in the securities business.

	1 - 24			25 - 99			100 and Over			Total		
	No.	%		No.	%		No.	%		No.	%	
Salesmen and Saleswomen	346	28.1		613	25.1		1,309	23.1		2,268	24.3	
Sales Trainees	12	0.9		47	1.9		134	2.4		193	2.1	
Trading:												
Bond Traders	54	4.4		77	3.2		148	2.6		279	3.0	
Stock Traders	53	4.3		125	5.1		190	3.4		368	3.9	
Other trading personnel	36	2.9		165	6.8		396	7.0		597	6.4	
Underwriters	8	0.6		27	1.1		65	1.1		100	1.1	
Analysis and Statisticians	12	1.0		67	2.7		105	1.9		184	2.0	
Other specialists	1	0.1		9	0.4		30	0.5		40	0.4	
Senior Administrative	227	18.5		252	10.3		340	6.0		819	8.8	
Accounting and Delivery Personnel	249	20.3		509	20.8		1,549	27.4		2,307	24.7	
All others	232	18.9		552	22.6		1,390	24.6		2,174	23.3	
Total Personnel	1,230	100.0%		2,443	100.0%		5,656	100.0%		9,329	100.0%	
Number of the above total who are shareholders (if a limited company or partners (if a partnership)	365	29.7%		426	17.4%		562	9.9%		1,353	14.5%	
Number of Members reporting	110			52			24			186		



PART 1 - EXHIBIT "B"

Page 1.

IDAC - PERSONNEL SURVEY - AUGUST 29, 1958

TABLE "A"

	No. of Staff 1-10	No. of Staff 11 - 25	No. of Staff 26 - 50	No. of Staff 51 - 100	No. of Staff 100 - 200	No. of Staff Over 200	Totals		
	%	%	%	%	%	%	%		
Number of firms in Group	66	56	30	26	9	9	196		
Shareholders and Partners	167 41.3	244	201	218	153	280	1,263	14.7	
All other staff	237 58.7	715	853	1,490	1,254	2,777	7,326	85.3	
Totals	404 100%	959	1,054	1,708	1,407	3,057	8,589	100%	

Note: 193 Member Firms responded
1 Member Firm did not respond
2 Member Firms filed combined returns for their investment firm
and stock affiliate.



PART I - EXHIBIT "B"

TABLE "B"

Number of Firms in Group	No. of Staff		No. of Staff		No. of Staff		No. of Staff		No. of Staff		No. of Staff		Totals	
	1 - 10	11 - 25	26 - 50	51 - 100	101 - 200	Over 200	9	9	9	9				
	66	56	30	26	9	196								
	%	%	%	%	%	%								
Salesmen	100	24.8	264	27.5	274	26.0	378	22.1	343	24.4	634	20.7	1,993	23.2
Saleswomen	3	.7	6	.6	6	.6	2	.1	8	.6	5	.2	30	.3
Sales Trainees	1	.2	12	1.3	19	1.8	31	1.8	32	2.3	62	2.0	157	1.8
Bond and Unlisted Stock Traders	24	5.9	48	5.0	46	4.4	76	4.4	45	3.2	99	3.2	338	3.9
Floor Traders	-	-	52	5.4	49	4.6	73	4.3	41	2.9	44	1.4	259	3.0
Underwriters	8	2.0	4	.4	20	1.9	14	.8	15	1.1	53	1.7	114	1.3
Analysts and Statisticians	2	.5	17	1.8	33	3.1	36	2.1	30	2.2	61	2.0	179	2.1
Accounting and Delivery Personnel	55	13.6	178	18.6	203	19.3	358	21.0	337	23.9	672	22.0	1,803	21.0
Other Specialists	-	-	2	.2	3	.3	15	.9	12	.9	23	.8	55	.7
Senior Administrative	116	28.7	143	14.9	131	12.4	155	9.1	71	5.0	107	3.5	723	8.4
All others	95	23.6	233	24.3	270	25.6	570	33.4	473	33.5	1,297	42.5	2,938	34.3
Totals	404	100%	959	100%	1,054	100%	1,708	100%	1,407	100%	3,057	100%	8,589	100%

PART I - EXHIBIT "C"CHANGES IN I.D.A.C. MEMBERSHIP: APRIL, 1955 - MARCH, 1962New Members - Resignations

1955 - 1956	4	4
1956 - 1957	1	8
1957 - 1958	8	5
1958 - 1959	1	9
1959 - 1960	7	9
1960 - 1961	7	4
1961 - 1962	3	8
	<u>31</u>	<u>47</u>

Reason for Resignation:

Going out of business (1)	20
Dual members resigning (2)	9
Dual members merging (2)	2
Business sold to another Member	7
Inability to meet I.D.A.C. requirements	5
Resigned and later rejoined	2
Business sold to new interests and character of business changed	2
	<u>47</u>

Notes:

(1) Death or retirement of a senior partner or senior partner or principal contributor of capital was the most common reason for going out of business. In many cases one or more of the partners or directors of the resigning firm eventually become associated with other member firms or corporations.

(2) At one time the Association had a number of "dual" memberships where both the investment dealing organization and the affiliated stock exchange organization held memberships. Changes in the way of doing business resulted in 9 stock exchange houses resigning. In two cases the stock business was merged with the investment business in one company.



DATE: _____

1955 - 1956	4	A
1956 - 1957	1	B
1957 - 1958	8	C
1958 - 1959	1	D
1959 - 1960	7	E
1960 - 1961	7	F
1961 - 1962	3	G
	<u>31</u>	<u>47</u>

Reason for Resignation:

- 20 (1) Going out of business
- 9 (2) Dual members resigning
- 2 (3) Dual members merging
- 7 Business sold to another Member
- 2 Inability to meet I.D.U. requirements
- 2 Resigned and later rejoined
- 2 Business sold to new interests and character of business changed

2
47

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At one time the Association had a number of "dual" memberships where both the investment dealing organization and the affiliated stock exchange organization held memberships. Changes in the way of doing business resulted in 2 stock exchange houses resigning. In two cases the stock business was merged with the investment business in one company.



Jerom. Ontario

* # Secret-ary and Treasurer

Comptroller

Office-Manager
PersonnelAccounting and
DeliveriesVice-President
Stocks

Block Stock

Arbitrage

Floor Traders

Order Dept.

Wire Room

Vice-President - Govt.
& Municipal Financing

Underwriting

Syndicating

Business Development

Research

* Portfolio Management

Vice-President
Corporation Financing

Underwriting

Syndicating

Business Development

Vice-President
Sales

* Ontario Branches

* Quebec Branches

* Western Branches

U.S. Sales

Vice-President
Trading

Bonds

Money Market

Unlisted Stocks

NOTES:

1. (*) indicates function usually in charge of a director. A director may be responsible for more than one function.

2. United States sales and stock business are frequently handled through an affiliated firm or corporation.

3. Some investment houses use an Executive Committee of the Board. Some houses designate the Senior Vice-President as Executive Vice-President.

4. Advertising brochures, etc. are usually the responsibility of an official in the sales or underwriting department.

5. (#) At least one Member has a Vice-President, Finance.



PART II

HISTORY

1. The Investment Dealers' Association of Canada was formed in June 1961 under the name Bond Dealers' Association of Canada. It was the result of a merger of a group of bond dealers in Montreal and the financial section of the City of Toronto Board of Trade.

2. The Association originally started with 32 Members, all except one having their Head Office located in either Toronto or Montreal. By 1920 the membership had grown to 104 firms, many with branches located across the country. The Association could be said by that date to have attained National stature. The name Bond Dealers' Association of Canada was felt not to be descriptive of the diverse and expanding business carried on by the Members of the Association. In 1925 the name was changed to The Investment Bankers' Association of Canada and the Members of the Association began to refer to themselves as Investment Bankers, thus following the nomenclature in general use in the United States.

3. In 1934 the Bank Act was changed and one of the amendments was to restrict to Chartered Banks the use of the names Bank or Banker. It was accordingly necessary to search for an alternative name for the Association to describe the type of business carried on by its Members. The term Investment Dealer was decided upon, the name of the Association became the Investment Dealers' Association of Canada and Members were encouraged to refer to themselves as Investment Dealers. The term



PART II

History

1. The Investment Dealers' Association of

Canada was formed in June 1901 under the name Bond Dealers' Association of Canada. It was the result of a merger of a group of bond dealers in Montreal and the financial section of the City of Toronto Board of Trade.

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The name Bond Dealers' Association of Canada was left not to be descriptive of the diverse and expanding business carried on by the Members of the Association. In 1925 the name was changed to The Investment Bankers' Association of Canada and the Members of the Association began to refer to themselves as Investment Bankers, thus following the nomenclature in general use in the United

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1 is now widely accepted in Canada and official recognition
2 has been given to it in the Securities Acts of several
3 of the Provinces.

4 4. By 1939 the Association had a membership
5 of 130 located across Canada and was in a favourable
6 position to co-operate with the Government in the
7 emergency of war. The National War Finance Committee
8 included a large number of Investment Dealers who played
9 a vital role in the financing of Canada's war effort.

10 5. Since the end of World War II the
11 Association has continued to grow and expand its scope.
12 After reaching a peak of 208 Members in 1958 the
13 membership has now levelled off, owing mainly to mergers
14 and buy-outs, to 189 Members. Although some slight
15 reduction of this number may be expected, the outlook for
16 the foreseeable future is that this approximate
17 membership will be maintained. Exhibit A shows the
18 Members of the Association as at 31st January, 1962.

19 6. Since its inception, the Association's
20 Head Office has been maintained in Toronto. In 1947 a
21 Branch office was opened in Montreal to serve the needs
22 of the Members in that city and throughout the Province
23 of Quebec. This office has now become an essential part
24 of the Association and has done much to establish and
25 maintain its national character. Recently a French
26 translation of the Association's name has been approved
27 and Members in the Province of Quebec are encouraged to
28 make use of this name as well as the English version.

29 7. In 1947 an Education Programme was started
30 for the employees of Members and for the general public.



has been given to it in the Securities Acts of several of the Provinces.

4. By 1939 the Association had a membership of 130 located across Canada and was in a favourable position to co-operate with the Government in the inclusion of SAC. The National and Provincial Associations included a large number of Investment Dealers who played a vital role in the financing of Canada's war effort.

5. Since the end of World War II the Association has continued to grow and expand its scope. After reaching a peak of 208 Members in 1958 the membership has now levelled off, owing mainly to mergers and acquisitions. The outlook for the foreseeable future is that this approximate

membership will be maintained. Exhibit A shows the Members of the Association as at 31st January, 1962.

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7. In 1947 an education programme was started



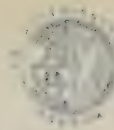
1 Two correspondence courses for employees and a number
2 of courses of various types for the public, are now
3 offered by the Association. Work on a third employee
4 course is at present in progress. In keeping with the
5 National aspect of the Association one of the employees'
6 courses and a number of the courses for the general public
7 are available in French, and all course assignments may
8 be answered in French.

9 STRUCTURE AND ORGANIZATION

10 (a) Constitution and By-Laws

11 8. Membership in the Association is governed
12 by its Constitution and By-laws. The Association is an
13 unincorporated non-profit body. The Constitution and
14 By-laws may from time to time be repealed, amended or
15 re-enacted by the National Executive Committee of the
16 Association, subject always to the approval of the Members
17 passed at a General or special meeting of the Association,
18 by an affirmative vote of two-thirds of the votes given
19 on such Resolution. They encompass the basic philosophy
20 and operations of the Association and allow the making
21 of Regulations pursuant to the by-laws for the day to day
22 operations of the Association and its Members.

23 9. The right to apply for Membership in the
24 Association is open to all individuals, firms or
25 corporations carrying on business in Canada as Investment
26 Dealers, provided that the business of the applicant is
27 of such character that at least half of the gross profits
28 of such business for the twelve month period immediately
29 prior to application resulted from, or consisted of,
30 the underwriting, distributing or buying and selling,



1945

of courses of various types for the public, are now
offered by the Association. Work on a third employee
course is at present in progress. In keeping with the
National aspect of the Association one of the employees'
courses and a number of the courses for the general public
are available in French, and all course assignments may
be answered in French.

STRUCTURE AND ORGANIZATION

(a) Constitution and By-Laws

8. Membership in the Association is governed
by its Constitution and By-Laws. The Association is an
unincorporated association. The Constitution and
By-Laws may from time to time be repealed, amended or
re-enacted by the National Executive Committee of the
Association, subject always to the approval of the Members
passed at a General or special meeting of the Association,
by an affirmative vote of two-thirds of the votes given
on such Resolution. They encompass the basic philosophy
and operations of the Association and allow the making
of Regulations pursuant to the By-Laws from day to day
operations of the Association and its Members.

9. The right to apply for Membership in the

Association is open to all individuals, firms or
concerns carrying on business in Canada as
Dealers, provided that the business of the applicant is
of such character that at least half of the gross profits
of such business for the twelve month period immediately
prior to application resulted from, or consisted of,



1 either as principal or agent, from and to the public in
2 Canada, of investment securities including bonds,
3 debentures, notes and shares of an investment character.
4 In addition, at least 50 per cent of the principals of
5 all applicants for Membership must have been in the
6 investment business for at least five years, and all
7 applicants must possess a minimum of \$25,000 liquid
8 capital plus such extra capital as may be required to
9 allow them to hold inventory, carry margin accounts and
10 carry on other operations necessary to their business.

11 10. An applicant for Membership in the
12 Association is first screened by the local District
13 Executive Committee, and providing it satisfies the
14 requirements of By-law No. 1 of the Association and is
15 approved by the Committee, notice of the application is
16 given to all Members who have a period of time in which
17 to object to the applicant. If there is no objection,
18 the application is referred to the National Executive
19 Committee for their final decision.

20 11. During the forty-six years of its
21 existence, the Association's By-laws have been continually
22 amended to reflect the changing standards and requirements
23 of the industry, and there have been periodic reviews
24 of the Membership requirements with particular reference
25 to standards of ethics, type of business transacted and
26 financial position.

27 12. Exhibit B contains the Constitution and
28 By-laws of the Association, and Exhibit C the Regulations
29 of the Association, except the Trading and Delivery
30 Regulations.



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requirements of By-law No. 1 of the Association and is

approved by the Committee, notice of the application is

given to all Members who have a period of time in which

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the application is referred to the National Executive

Committee for their final decision.

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amended to reflect the changing standards and requirements

of the industry, and there have been periodic reviews

of the Membership requirements with particular reference

to standards of ethics, type of business transacted and

12. Exhibit B contains the Constitution and

By-laws of the Association, and Exhibit C the Regulations

of the Association, except the Trading and Delivery



1 (b) Organization

2 13. The Investment Dealers' Association of
3 Canada is a National organization, but in keeping with
4 the size and diversity of Canada it is divided into six
5 Districts, as follows: Atlantic District (Provinces of
6 Newfoundland, New Brunswick, Nova Scotia and Prince
7 Edward Island); Quebec District (Province of Quebec);
8 Ontario District (Province of Ontario); Mid-Western
9 District (Provinces of Manitoba and Saskatchewan);
10 Alberta District (Province of Alberta); and Pacific
11 District (Province of British Columbia). Each district
12 is under the direction of a Chairman and District Executive
13 Committee, the District Chairmen being Vice-Presidents
14 of the Association and comprising, along with the
15 President and Immediate Past President, the National
16 Executive Committee. In addition, each district has a
17 District Business Conduct Committee comprised of the
18 District Chairman, the past five District Chairmen still
19 active in the investment business, and the Managing
20 Director. Appeal lies from this Committee to the National
21 Business Conduct Committee which is made up of the
22 Immediate Past President and the four previous Past
23 Presidents still active in the business. The Association
24 and each District appoints auditors and the Association
25 retains Counsel in Toronto and Montreal.

26 14. The permanent Executive staff of the
27 Association is made up of a Managing Director, Secretary-
28 Treasurer, Director of Education, Regional Director and
29 Secretary Emeritus.

30 15. Exhibit D lists the Officers, Committees

13. The Investment Dealers' Association of Canada is a national organization, but in keeping with the size and diversity of Canada it is divided into six Districts, as follows: Atlantic District (Provinces of Newfoundland, New Brunswick, Nova Scotia and Prince Edward Island); Quebec District (Province of Quebec); Ontario District (Province of Ontario); Mid-Western District (Provinces of Manitoba and Saskatchewan); Alberta District (Province of Alberta); and Pacific District (Province of British Columbia). Each district is under the direction of a Chairman and District Executive Committee, the District Chairman being Vice-President of the Association and comprising, along with the President and Immediate Past President, the National Executive Committee. In addition, each district has a District Business Conduct Committee comprised of the District Chairman, the past five District Chairmen still active in the investment business, and the Managing Director. Appeal lies from this Committee to the National Business Conduct Committee which is made up of the Immediate Past President and the four previous Past Presidents still active in the business. The Association and each District appoints auditors and the Association retains Counsel in Toronto and Montreal.

14. The permanent Executive staff of the Association is made up of a Managing Director, Secretary-Treasurer, Director of Education, Regional Director and



1 and Auditors of the Association for the year 1961-62 and
2 the Past Presidents of the Association since its
3 inception.

4 (c) Comparison With United States
5 and United Kingdom Associations

6 16. The Investment Dealers' Association of
7 Canada is not directly comparable to securities
8 organizations or associations in other countries. Although
9 in their early days the Investment Bankers Association of
10 America and The Investment Dealers' Association of Canada
11 were similar in their function, over the years the two
12 Associations have developed along somewhat divergent
13 lines.

14 17. Membership in the Investment Bankers
15 Association of America represents only a small percentage
16 of the securities dealers in that country (approximately
17 15 per cent of the nearly 5,000 securities dealers). In
18 the United States there is Federal Securities Legislation
19 in addition to the Securities Legislation in the various
20 States and membership in the U.S. Federal Government
21 sponsored and controlled National Association of
22 Securities Dealers is compulsory for all securities houses
23 in the country. The Investment Dealers' Association
24 of Canada performs some of the functions of both these
25 Associations. In Canada there is no Federal Securities
26 Legislation other than companies legislation and the
27 Securities Acts under which Investment Dealers operate
28 are provincial statutes. In the Securities Acts of the
29 Provinces of Ontario, Alberta and Saskatchewan, the
30 Association is specifically referred to, and is given



(115)

THE INVESTMENT OF THE ASSOCIATION FOR THE YEAR 1914

the Past Presidents of the Association since its

inception.

(c) Comparison With United States
AND OTHER INVESTMENT ASSOCIATIONS

16. The Investment Dealers' Association of

the United States and its branches in other countries

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in their early days the Investment Bankers Association of

America and The Investment Dealers' Association of Canada

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and provincial statutes. In the Securities Acts of the

Provinces of Ontario, Alberta and Saskatchewan, the

Association is specifically referred to, and its given



1 certain rights and responsibilities thereunder. A number
2 of other Provincial Securities Acts are at present
3 under review, and it seems likely, in at least one other
4 Province, that the Association will be granted similar
5 rights and responsibilities.

6 18. In the United Kingdom there is no
7 organization or association comparable to The Investment
8 Dealers' Association of Canada. The Issuing Houses
9 Association performs a somewhat similar function in the
10 field of new issue underwritings. There, however, any
11 comparison ends. The secondary market in securities
12 owned as principal, is, in the United Kingdom, carried on
13 by jobbers, and these firms come under the control of
14 the London or other Stock Exchange on which they operate.

15 FUNCTIONS

16 19. The principal functions of The Investment
17 Dealers' Association of Canada are as follows:
18 (i) Protection of the Investing Public;
19 (ii) Mutual Protection of Members;
20 (iii) Maintenance of High Ethical Standards;
21 (iv) Maintenance of Orderly Marketing and Trading;
22 (v) Education of Members' Employees and the Public;
23 (vi) Provision of Statistical Data;
24 (vii) Publications;
25 (viii) Liaison with Other Financial Institutions.

26 (i) Protection of the Investing Public

27 20. Investment Dealers are conscious of their
28 responsibilities to the investing public, both to
29 institutions and to the ordinary citizen. They endeavour
30 to maintain highest standards of ethics and reliability,

rights and responsibilities thereunder. A number of Provincial Securities Acts are at present in force, and the Commission is in the process of preparing a model Act for the provinces.

18. In the United Kingdom there is no organization or association comparable to the Investment Association of Canada. The Association performs a somewhat similar function in the field of new issues underwritings. There, however, any company desiring to issue securities in the United Kingdom, must first obtain approval from the Investment Association, and these firms come under the control of the London or other Stock Exchanges on which they operate.

19. The principal functions of the Investment

- Designs Association of Canada are as follows:
- (i) Protection of the Investing Public;
 - (ii) Mutual Protection of Members;
 - (iii) Maintenance of High Ethical Standards;
 - (iv) Maintenance of Orderly Marketing and Trading;
 - (v) Education of Members, Employees and the Public;
 - (vi) Provision of Statistical Data;
 - (vii) Publications;

20. Investment Dealers are members of the Association of the Investing Public.



1 and to ensure that all members of the public receive expert
2 advice and completely fair treatment. The Association
3 attaches the greatest importance to this.

4 21. At all times the Association has
5 endeavoured to keep the interests of the nation and the
6 investing public to the forefront. The Association has
7 been outspoken in its attempts to ensure that investors
8 are fairly and equitably treated by Corporations and
9 Governments alike, particularly during financial re-
10 organizations.

11 22. In particular, the Association controls in
12 its By-laws and Regulations the type of business carried
13 on by its Members or to be carried on by new Members,
14 and the minimum financial requirements of its Members or
15 of new Members.

16 23. (a) Type of Business - The by-laws
17 require that all Members of the Association and applicants
18 for membership, must derive at least 50 per cent of their
19 profits from the underwriting, distributing, or buying
20 and selling, either as principal or agent, from and to
21 the public in Canada, of investment securities (including
22 bonds, debentures, notes and shares of an investment
23 character) as defined in the By-laws. At the discretion
24 of the applicable District Executive Committee, a Member
25 (or applicant) may submit its dollar volume rather than
26 profits. Applicants who have not been in business in
27 Canada for at least one year may be admitted to membership
28 on an estimate of their proposed business, but are liable
29 to six-monthly reviews on the type of business they
30 conduct for two years after admission to the Association.



and to ensure that all members of the public receive expert advice and completely fair treatment. The Association attaches the greatest importance to this.

21. At all times the Association has endeavoured to keep the interests of the nation and the investing public to the forefront. The Association has been outspoken in its attempts to ensure that investors are fairly and equitably treated by corporations and

22. In particular, the Association controls its By-laws and Regulations the type of business carried on by its Members or to be carried on by new Members, and the minimum financial requirements of its Members or of new Members.

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1 All members are liable to periodic routine reviews on
2 the type of business they conduct, and at the discretion
3 of either the National Executive Committee or the
4 applicable District Executive Committee may be required
5 to submit special reviews.

6 24. The By-Laws define investment securities
7 to include (i) government, municipal, hospital, school,
8 corporations and religious institutions, bonds, debentures,
9 notes and other securities not in default of principal or
10 interest; (ii) preferred shares not in arrears of
11 dividends; (iii) such common shares with demonstrated
12 earning power whether or not dividend paying, such shares
13 in Investment Companies, and such other securities as
14 the applicable District Executive Committee, with the
15 concurrence of the National Executive Committee, may from
16 time to time approve as investment securities.

17 25. Exhibit E consists of the Application for
18 Membership form and the form used when requiring Members
19 to submit a breakdown of the type of their business.

20 26. (b) Minimum Financial Requirements - All
21 Members of the Association are required to maintain
22 minimum capital in accordance with the type and magnitude
23 of operations carried on. The minimum liquid capital
24 which is to be maintained must be at least \$25,000, but
25 this has to be supplemented, and such liquid capital
26 must be at least sufficient to provide an adjusted liquid
27 capital equal to the sum of

28 (i) 2% of the Members' current liabilities or

29 \$50,000 whichever is less;

30 (ii) 2% of the Member's adjusted liabilities;

All members are liable to periodic routine reviews on

the type of business they conduct, and at the discretion

of either the National Executive Committee or the

applicable District Executive Committee may be required

to submit special reviews.

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this has to be supplemented, and such liquid capital

must be at least sufficient to provide an adjusted liquid

capital equal to the sum of

(1) 2% of the Members' current liabilities or

\$50,000 whichever is less;



(iii) Such additional amount as may be required if a Member does not deposit all clients' free credit balances in a Clients' Trust Account or carries margin accounts for clients or sells securities on an instalment payment plan.

In the case of a large national or international house carrying on a fully diversified Investment Dealers' business, the total amount of minimum capital required would be very substantial. Members are obliged to segregate clients' securities held in safekeeping from their own securities, and to carry minimum insurance coverage.

27. By-law 8A of the Association and the Regulations of the National Executive Committee made pursuant thereto, outline the minimum capital requirements of the Association. By-law 8C and the Regulations of the National Executive Committee made pursuant thereto, contain the insurance requirements of the Association. (Refer to Exhibits B and C).

(ii) Mutual Protection of Members

28. In common with other trade associations, one function of The Investment Dealers' Association of Canada is the protection of its Members. Every effort is made to foster the interests of the Investment Dealer, and the Association, when required, submits briefs and recommendations on behalf of the industry to the appropriate authorities.

(iii) Maintenance of High Ethical Standards

29. The speed at which securities transactions



and additional amounts as may be required
if a Member does not deposit all clients'
funds available in a liquid form.
Account or carries margin accounts for
clients or sells securities on an installment
payment plan.

In the case of a large national or international house
carrying on a fully diversified Investment Dealers'
business, the total amount of minimum capital required
would be very substantial. Members are obliged to
aggregate clients' securities held in safekeeping from
their own securities, and to carry minimum insurance
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Regulations of the National Executive Committee made
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the National Executive Committee made pursuant thereto,
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and the Association, when required, submits briefs and
recommendations on behalf of the industry to the
appropriate authorities.

(iii) Maintenance of High Ethical Standards



1 take place makes it impractical for each sale or purchase
2 to be confirmed in writing at the time. Shares or bonds
3 are bought and sold by word of mouth, either personally
4 or over the telephone, and although confirmed by letter
5 as soon as possible (usually the same day) this confirm-
6 ation is not received by the other party until the next
7 day at the earliest. However, failure to honour these
8 verbal contracts is extremely rare, and the word of an
9 Investment Dealer is regarded as his bond.

10 30. Although Members of the Investment Dealers'
11 Association of Canada have built up an enviable record
12 for their ethics, nevertheless infringements of ethics or
13 of the Association's Rules and Regulations do take place.
14 A District Business Conduct Committee is set up in each
15 District to hear and investigate fully any complaints
16 against Members of the Association. Not only is the
17 structure of these committees such that only senior
18 members of the industry serve on them, but in all
19 important matters the opinion of counsel is sought, thus
20 helping to ensure that the Rules and Regulations of the
21 Association are fairly and impartially enforced and that
22 high ethical standards are maintained. There is appeal
23 to the National Business Conduct Committee, which consists
24 of five Past Presidents of the Association.

25 31. The Association feels, particularly since
26 the amendments to the Disciplinary By-laws in October,
27 1961, that all complaints against Members have been
28 quickly and fairly dealt with by the appropriate committee
29 or committees. In the past two years two Members of the
30 Association have been suspended and three Members have



take place makes it impractical for each sale or purchase to be confirmed in writing at the time. Shares or bonds are bought and sold by word of mouth, either personally or over the telephone, and although confirmed by letter as soon as possible (usually the same day) this confirmation is not received by the other party until the next day at the earliest. However, failure to honour these verbal contracts is extremely rare, and the word of an investment dealer is regarded as sacrosanct.

30. Although Members of the Investment Dealers Association of Canada have built up an enviable record for their ethics, nevertheless infringements of ethics or of the Association's Rules and Regulations do take place. A District Business Conduct Committee is set up in each District to hear and investigate fully any complaints against Members of the Association. Not only is the structure of these committees such that only senior members of the industry serve on them, but in all important matters the opinion of counsel is sought, thus helping to ensure that the Rules and Regulations of the Association are fairly and impartially enforced and that high ethical standards are maintained. There is appeal to the National Business Conduct Committee, which consists of five past Presidents of the Association.

31. The Association feels, particularly since the amendments to the Disciplinary by-laws in October, 1961, that all complaints against Members have been quickly and fairly dealt with by the appropriate committee or committees. In the past two years two Members of the Association have been warned and three Members have



1 been fined.

2 (iv) Maintenance of Orderly Marketing and Trading

3 32. The Investment Dealers' Association of
4 Canada exercises the ultimate responsibility for the
5 manner in which secondary trading in Treasury Bills,
6 bonds, debentures and unlisted shares in Canada is
7 conducted. Day to day control over this trading is
8 exercised respectively in Toronto and Montreal by the
9 Toronto Bond Traders' Association and the Montreal Bond
10 Traders' Association. These two associations are
11 composed of representatives of Investment Dealers,
12 Chartered Banks and certain other financial organizations.

13 33. Both Bond Traders' Associations are
14 subsidiary to The Investment Dealers' Association of
15 Canada and agree in their By-laws or Regulations to be
16 bound by the decisions of the Association as regards to
17 unlisted trading. In practice, all routine matters are
18 handled by the committees of the two Bond Traders'
19 Associations, whose decisions are normally final. However,
20 any Member of The Investment Dealers' Association of
21 Canada who is dissatisfied with a ruling of one or other
22 of the Bond Traders' Associations is entitled to bring the
23 matter before the District Executive Committee of The
24 Investment Dealers' Association of Canada who, through their
25 Bond Traders' Liaison sub-committee, would investigate
26 the matter. The Bond Traders' Associations make such
27 rules and regulations as they feel necessary and desirable
28 for orderly trading, and although these provisionally go
29 into force when passed, they are referred to The Investment
30 Dealers' Association of Canada for confirmation, and if not



32. The Investment Dealers' Association of Canada

Canada exercises the ultimate responsibility for the manner in which secondary trading in Treasury Bills, bonds, debentures and listed shares in Canada is conducted. Day to day control over this trading is exercised respectively in Toronto and Montreal by the Toronto Bond Traders' Association and the Montreal Bond Traders' Association, both of which are composed of representatives of Investment Dealers, Chartered Banks and certain other financial organizations.

33. Bond Traders' Associations and

subordinate to The Investment Dealers' Association of Canada and agree in their By-laws or Regulations to be bound by the decisions of the Association as regards to listed trading. In practice, all routine matters are handled by the committees of the two Bond Traders' Associations, whose decisions are normally final. However

any member of The Investment Dealers' Association of Canada who is dissatisfied with a ruling of one or other of the Bond Traders' Associations is entitled to bring the matter before the District Executive Committee of The Investment Dealers' Association of Canada who, through the Bond Traders' Liaison and Committee, would have regard to the matter. The Bond Traders' Associations make such rules and regulations as they feel necessary and desirable. Information when passed, may be referred to The Investment



so confirmed would lapse.

34. Exhibit F contains the Trading and Delivery Regulations of The Investment Dealers' Association of Canada.

35. The Investment Dealers' Association of Canada maintains close liaison and contact with the Government of Canada, the Bank of Canada, and the Provincial Governments and Securities Commissioners. This contact is not only established and maintained by the elected Officers immediately on taking office, but is maintained on a continuing basis by the Managing Director and other permanent Officers of the Association.

(v) Education of Members' Employees and the Public

36. From its inception in 1947, the I.D.A.C. education programme has been rapidly expanded and now covers two distinct areas. A comprehensive internal education programme has been developed to speed the training of new employees within the industry in many of the complexities of the investment business and thereby to equip them to serve the public better. An external education programme has also been developed to acquaint the Canadian investing public with the fundamental terms, procedures and principles of sound investment management. The Association employs a full-time education officer to direct both programmes.

(a) Internal Education

37. The Association's internal education programme is founded on two correspondence courses entitled "Principles and Practices of Investment Finance in Canada." Both courses were written by experts in the



11 so confirmed would lapse.

12 32. While it is true that the Association and its

13 members are not a "body" or "association" of

14 persons,

15 33. The Investment Dealers' Association of

16 Canada maintains close liaison and contact with the

17 Government of Canada, the Bank of Canada, and the

18 Provincial Governments and Securities Commissioners. This

19 contact is not only established and maintained by the

20 elected Officers immediately on taking office, but is

21 maintained on a continuing basis by the Managing Director

22 and other permanent Officers of the Association.

23 (c) Education of Investors and the Public

24 34. From its inception in 1947, the I.D.A.C.

25 education programme has been rapidly expanded and now

26 covers two distinct areas. A comprehensive internal

27 education programme has been developed to speed the

28 training of new employees within the industry in many of

29 the complexities of the investment business and thereby

30 to equip them to serve the public better. An external

31 education programme has also been developed to acquaint

32 the Canadian investing public with the fundamental terms,

33 procedures and principles of sound investment management.

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35 direct both programmes.

36 (d) Internal Education

37 35. The Association's internal education

38 programme is founded on two correspondence courses

39 entitled "Principles and Practices of Investment Finance

40 and



1 industry and both are revised and have new assignment
2 questions added each year. Course I is designed for all
3 new employees of Member firms, though it is also made
4 available to members of most other financial institutions
5 and to financial employees of Canadian corporations. It
6 covers such topics as elementary accounting, the
7 interpretation of financial statements, the character-
8 istics of various types of investment securities, the
9 origination and trading of securities, I.D.A.C.
10 regulations and the Provincial Securities Acts. Course
11 II is at present restricted to employees of Investment
12 Dealers, members of Canadian stock exchanges and editorial
13 employees of the financial press. This course leads the
14 student into more detailed financial analysis and covers
15 corporate, provincial and municipal underwriting and
16 security distributor; the operations of the Bank of
17 Canada; the money market; portfolio management and
18 salesmanship.

19 38. The material for these two courses is
20 mailed to students at regular intervals during the year
21 and within a specified time completed assignments must
22 be submitted. These are marked and graded and at the
23 end of each Course there is a compulsory examination.
24 To date, with some 5,996 persons having enrolled in the
25 two courses, a total of 3,601 have successfully completed
26 the programmes. Exhibit G shows the cumulative record of
27 course results.

28 39. At the time of writing, a third course for
29 Members' employees is being prepared. This course will
30 outline the banking, accounting, contractual, regulatory



industry and both are revised and have new assignments
questions added each year. Course I is designed for all
new employees of Member firms, though it is also made
available to members of most other financial institutions
and to financial employees of Canadian corporations. It
covers such topics as elementary accounting, the
interpretation of financial statements, the character-
istics of various types of investment securities, the
origination and trading of securities, I.D.A.C.
regulations and the Provincial Securities Acts. Course
II is at present restricted to employees of Investment
Dealers, members of Canadian stock exchanges and editorial
employees of the financial press. This course leads the
student into more detailed financial analysis and covers
corporate, provincial and municipal underwriting and
security distribution; the operations of the Bank of
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two courses, a total of 3,601 have successfully completed
the programmes. Exhibit G shows the cumulative record of

39. At the time of writing, a third course for
Members' employees is being prepared. This course will



1 and legal aspects of the investment business.

2 (b) External Education

3 40. Each year the Association prints and
4 distributes to the general public a revised edition of
5 its Home Study Correspondence Course "How to Invest Your
6 Money in Bonds and Stocks." This course covers such
7 subjects as bonds and debentures, preferred and common
8 shares, the interpretation of financial statements and
9 portfolio management. At present, the course is
10 distributed to the public through the Universities of
11 Western Ontario and Saskatchewan in English, and Laval
12 University in French. It has received wide distribution
13 both in Canada and abroad. A total of some 18,000
14 persons have enrolled in the English language version and
15 approximately 2,000 in the French edition. Commencing
16 September, 1962 the Association itself intends to take
17 over distribution of the English edition of the course in
18 an attempt to obtain even wider public distribution.

19 41. The Association maintains across the
20 country active voluntary Speakers' Panels composed of
21 Members' employees. Speeches are given on request to a
22 large number of organizations including universities,
23 schools, service clubs, women's associations, trade and
24 professional bodies. About 100 public addresses have
25 been arranged by the Association during the past year.

26 42. In 1954 the Association produced a film
27 entitled "A Matter of Importance." It stresses the
28 importance of an investment programme to a typical young
29 Canadian family. This film is available to Members of
30 the Speakers' Panel where it has received over 300

and legal aspects of the investment business.

(a) Investment Education

40. Each year the Association prints and

distributes to the general public a revised edition of its Home Study Correspondence Course "How to Invest Your Money in Bonds and Stocks." This course covers such subjects as bonds and debentures, preferred and common shares, the interpretation of financial statements and portfolio management. At present, the course is

distributed to the public through the Universities of Western Ontario and Saskatchewan in English, and Laval University in French. It has received wide distribution both in Canada and abroad. A total of some 18,000

persons have enrolled in the English language version and approximately 2,000 in the French edition. Commencing September, 1962 the Association itself intends to take over distribution of the English edition of the course in an attempt to obtain even wider public distribution.

41. The Association maintains across the

country active voluntary Speakers' Panels composed of Members' employees. Speeches are given on request to a

large number of organizations including universities, schools, service clubs, women's associations, trade and professional bodies. About 100 public addresses have been arranged by the Association during the past year.

42. In 1954 the Association produced a film

entitled "A Matter of Importance." It stresses the importance of an investment programme to a typical young Canadian family. This film is available to Members of



1 showings. It has also been widely screened on television
2 across the country.

3 43. Our public educational programme also
4 includes lecture courses for employees of Canadian
5 companies and evening lecture courses for the general
6 public held in co-operation with a number of Canadian
7 universities, school boards and other educational
8 bodies. Exhibit H shows that over 1,700 Canadians were
9 enrolled in these courses during the past year.

10 44. In the Spring of the past seven years the
11 Association has co-operated with the Toronto and Montreal
12 Stock Exchanges in week-long visits of staff members of
13 the commerce and finance departments of Canadian
14 universities. This programme has given over 50 Canadian
15 university professors an intimate glimpse of the
16 operations of Member firms and helped to broaden their
17 understanding of the investment industry's role in the
18 continued growth of our economy.

19 45. For the past few years several of our
20 larger Members have also played host to visiting high
21 school teachers and guidance counsellors. These visits
22 have helped acquaint the teachers with career opportuni-
23 ties in the investment business for their commercial
24 and business graduates and assisted the industry in
25 recruiting promising junior personnel.

26 (vi) Provision of Statistical Data

27 46. Apart from an employee survey completed
28 in 1958 and several surveys conducted in preparation for
29 this Brief, the Association has attempted little in the
30 way of gathering statistical data on the operations of

showings. It has also been widely screened on television across the country.

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ties in the investment business for their commercial

and business graduates and assisted the industry in

recruiting promising junior personnel.

(v) Training of Personnel

46. Apart from an employee survey completed

in 1958 and several surveys conducted in preparation for

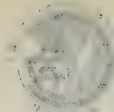
this Brief, the Association has attempted little in the



1 its Members. This failure has been the result of the
2 formidable problems involved in gathering reliable
3 statistical information. It has become apparent that no
4 two firms within the Association keep their books in the
5 same way. For example: fiscal-year-ends among our
6 Members fall throughout the calendar year; some firms
7 record sales on transaction dates, others on delivery
8 dates; and no two firms have precisely the same business
9 "mix" between the institutional, retail, money market,
10 bond and stock aspects of their business.

11 47. The Association is hopeful, however, that
12 a full and accurate statistical picture of the industry
13 will soon emerge. A recent request from the Dominion
14 Bureau of Statistics for further factual data as well as
15 similar requests from the present Royal Commission have
16 made many Members aware of the poverty of statistical
17 information presently available and the value it would
18 have for all concerned. The Association's new education
19 course currently under development is also expected to
20 help in standardizing accounting practices within the
21 industry and make regular statistical collection and
22 periodic statistical reviews more readily obtainable.

23 48. Nevertheless, since 1960 the Association
24 has collected from its Members, through its District
25 Auditors, a total of Members' borrowings outside the
26 banking system and the Bank of Canada by any method on the
27 collateral of securities owned by the Member, including
28 day-to-day, call and term loans, buy-backs and re-
29 purchase agreements where the aggregate total of such
30 borrowing is in excess of \$500,000. These totals are



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purchase agreements where the aggregate total of such



1 available to Members on request every Friday morning.
2 They are also released on a confidential basis to the
3 Bank of Canada, the Department of Finance and the Dominion
4 Bureau of Statistics.

5 49. Similarly, the Association co-operates with
6 the Dominion Bureau of Statistics in obtaining, assembling
7 and distributing statistics showing the sales and
8 purchases of securities between Canada and other countries.
9 These are reproduced and circulated to all Members of the
10 Association. For an example, see Exhibit I.

11 50. Each business day, the bid and asked
12 quotations on leading corporation, government and overseas
13 bonds are gathered from Member firms and distributed
14 nationally to the financial press. Weekly reports on
15 the domestic bond market are also supplied to Canadian
16 Press and the Canadian Broadcasting Corporation.

17 (vii) Publications

18 51. For the convenience of its Members, the
19 Association maintains a Directory of Members brought up-
20 to-date twice yearly. This Directory lists all the
21 Members of the Association with their branches, wire
22 communications, partners, officers and directors.
23 Exhibit J is the Association's Directory of Members.

24 52. The Association currently issues four
25 other publications for distribution to Members and to the
26 general public. These are as follows:

27 * "Canada and Canadian Provinces,
28 Funded Debts Outstanding" - This
29 book is published annually with half
30 yearly supplements and at present about



...to be made available to the public.

They are also released on a confidential basis to the

Bank of Canada, the Department of Finance and the Dominion

Bureau of Statistics.

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* "Canada and Canadian Provinces,

Round Dots Outstanding" - This

book is published annually with half

...



1 17,000 copies of each are

2 distributed each year.

3 * "How to Read Financial Statements" -

4 Designed for the novice investor,

5 this publication first appeared in

6 1958 and over 42,000 copies have now

7 been distributed.

8 * "Investment Terms and Definitions" -

9 Also for the novice investor, this

10 booklet has been in print, with

11 periodic revisions, for over 15 years.

12 Some 60,000 copies of it have now been

13 distributed.

14 * "A Career in Finance" - This

15 publication tells the high school

16 and university graduate about career

17 opportunities in the investment

18 industry. It has recently been

19 completely rewritten and 15,000 copies

20 of the new version are now being

21 printed.

22 Exhibit K contains copies of these four publications.

23 (viii) Liaison with Other Financial Institutions

24 53. The Investment Dealers' Association of

25 Canada maintains liaison with the leading Stock Exchanges

26 in the country. Three districts (Quebec, Ontario and

27 Pacific) maintain Stock Exchange Liaison sub-committees

28 and consultation with the local Stock Exchanges takes

29 place on matters concerning the functioning of the

30 financial industry.



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 Also for the novice investor, this
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 1958 and over 45,000 copies have now
 this publication first appeared in
 Designed for the novice investor,
 * "How to Read Financial Statements" -
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 17,000 copies of each are



54. The Association also liaises and maintains contact with The Canadian Bankers' Association, The Trust Companies Association of Canada, The Dominion Mortgage and Investments Association, The Canadian Life Insurance Officers Association and other Associations in Canada concerned with the investment industry.

55. Abroad, the Association maintains contact and exchange of information with the Investment Bankers Association of America, and some 32 Members of the Association are also Members of the Investment Bankers Association of America.

Trends and Indications for the Future

56. In the years ahead the Association intends to expand and refine its internal education programme to equip employees of Member firms to serve the public better. Moves towards a broader programme of public education may also be expected. To strengthen the protection given to the investing public, the Association intends to maintain and improve its Members' standard of ethics and type of business by further tightening of existing regulations on membership and discipline. Finally, the Association hopes to embark on a fuller and more regular programme of statistical collection and reporting which should assist our Members, government bodies and other interested parties in understanding the ever-changing nature of our business.

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PART II

THE I.D.A.C. - EXHIBIT D

PAGE 1.

OFFICERS AND COMMITTEES

of

The Investment Dealers' Association
of Canada

Head Office
55 Yonge Street, Toronto

Regional Office
132 St. James Street West, Montreal

OFFICERS 1961-62

President
Arthur J. Milner
Mills, Spence & Co. Limited, Toronto

Vice-Presidents

J. William Ritchie, Eastern Securities Company Limited Halifax.	D.J. Langill, W.C. Pitfield & Company Limited, Winnipeg
---	---

W.M. Reay, Nesbitt, Thomson and Company, Limited, Montreal.	K.M. Johnston, Wood, Gundy & Company Limited, Calgary
---	---

D.S. Beatty, Burns Bros. & Denton Limited, Toronto	Ross Wilson, A.E. Ames & Co. Limited Vancouver.
--	---

Immediate Past-President

Honorary President

Eric S. Morse, W.C. Pitfield & Company Limited	C.L. Gundy, Wood, Gundy & Company Limited, Toronto.
---	---

Honorary Vice-President

Honorary Treasurer

J.R. Hughes, Royal Securities Corporation Limited, Montreal.	J. Edgar Hill, Royal Securities Corporation Limited, Montreal.
--	---

Managing Director

Assistant Director
of Education

H.L. Gassard, The Investment Dealers' Association of Canada, Toronto	Eric A. Harvie, The Investment Dealers' Association of Canada, Toronto.
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Committee
of the

1940

THE INVESTMENT DEALERS' ASSOCIATION

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OFFICERS AND COMMITTEES

The Investment Dealers' Association
of Canada

1940

55 Yonge Street, Toronto

Regional Office

132 St. James Street West, Montreal

OFFICERS 1941-42

President

Arthur J. Milner

Mills, Spence & Co. Limited, Toronto

Vice-Presidents

J. William Ritchie,

Halifax Scientific Company Limited,
Halifax, Nova Scotia

W.M. Reay,

Maritime Transport and Storage
Limited, Montreal

J.C. Bessie,

James Bros. & Denton Limited,
Toronto

Executive Committee

Eric S. Morse,

W.C. Pittfield & Company Limited
Limited, Toronto

Honorary Vice-President

J. R. W. ...

Royal Securities Corporation
Limited, Montreal

J. Edgar Hill,

Royal Securities
Corporation Limited,
Montreal

Managing Director

Assistant Director
of Education

Eric A. Harris,

The Investment Dealers' Association
of Canada, Toronto



THE I.D.A.C. - EXHIBIT D

PAGE 2

Secretary-Treasurer Regional Director

W.S. Walter, L.F. Almond,
The Investment Dealers' The Investment Dealers'
Association of Canada, Association of Canada,
Toronto. Montreal.

Secretary Emeritus Counsel

J.A. Kingsmill, R.O. Daly, Q.C.,
The Investment Dealers' Daly, Harvey & Cooper,
Association of Canada, Toronto.
Toronto.

Auditors
Bakins and MacDonald,
Toronto. G.B. Foster, Q.C.,
Foster, Hannan, Watt,
Leggat & Colby,
Montreal.

NATIONAL EXECUTIVE COMMITTEE

(The President, the Vice-Presidents and
the Immediate Past President comprise
the National Executive Committee).

ARTHUR J. MILNER, Toronto D.J. LANGILL, Winnipeg
J. WILLIAM RITCHIE, Halifax K.M. JOHNSTON, Calgary.
W.M. REAY, Montreal. ROSS WILSON, Vancouver.
D.S. BEATTY, Toronto. ERIC S. MORSE, Montreal.

Secretary-Treasurer

General Manager

V.S. HARRIS,
The Investment Dealers'
Association of Canada,
Toronto.

L.R. ALMOND,
The Investment Dealers'
Association of Canada,
Montreal.

Secretary Emeritus

Chairman

J.A. KENNEDY,
The Investment Dealers'
Association of Canada,
Toronto.

R.C. DAVIS, D.D.,
Davis, Harvey & Cooper,
Toronto.

EAKINS and MacDONALD,
Toronto.

J.B. GORDON, M.D.,
Gordon, Gordon & Goby,
Montreal.

NATIONAL EXECUTIVE COMMITTEE

(The following are the Vice-Presidents and
the Immediate Past President comprise
the National Executive Committee).

ARTHUR J. MILLER, Toronto	D.J. FANLIE, Winnipeg
J. WILLIAM RITCHIE, Halifax	A.M. LEBLANC, Montreal
R.W. BRY, Montreal	ROSS WILSON, Vancouver
D.S. BEATTY, Toronto	ERIC S. MORSE, Montreal



THE I.D.A.C. - EXHIBIT D

PAGE 3

DISTRICT EXECUTIVE COMMITTEES, 1961-62

ATLANTIC DISTRICT

J. William Ritchie, Chairman	Eastern Securities Company Limited...Halifax.
H.D. Scully, Vice-Chairman	Nesbitt, Thomson and Company, Limited... Saint John.
C.E. Asprey	F.J. Brennan & Company Limited...Charlottetown
Adrian Bridgehouse	Gairdner & Company Limited...Halifax
Gerald R. Coyle, Secretary-Treasurer	Wood, Gundy & Company Limited...Halifax
J.D. Inches	Royal Securities Corporation Limited...Saint John.
William C. Lee	Stanbury & Company LimitedHalifax
D.C. MacKay	W.C. Pitfield & Company, Limited...Saint John
W.P. MacMurray	Eastern Securities Company Limited...Saint John.
John M. Robinson	W.C. Pitfield & Company, Limited...Halifax
Elliott Spafford	Cornell, Macgillivray Limited....Halifax
J.A. MacMurray, Ex-officio	Eastern Securities Company Limited....Saint John

QUEBEC DISTRICT

W.M. Reay, Chairman	Nesbitt, Thomson and Company, Limited..Montreal
J.P.W. Ostiguy, Vice-Chairman	Morgan, Ostiguy & Hudon Ltd...Montreal
H.W. Andrews	Graham, Armstrong Securities Ltd...Montreal
B.E. de Breyné	L.G. Beaubien & Co. Limited...Montreal
M. David	Credit Interprovincial Inc....Montreal



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THE I.D.A.G. - EXHIBIT D

DISTRICT EXECUTIVE COMMITTEE, 1961-62

ATLANTIC DISTRICT

W. Williams, Chairman	W. Williams, Chairman
H.D. Scully, Vice-Chairman	H.D. Scully, Vice-Chairman
G.E. Adams	G.E. Adams
Adrian Bridgehouse	Adrian Bridgehouse
Detain A. Doyle	Detain A. Doyle
W.D. Inches	W.D. Inches
William G. Lee	William G. Lee
D.D. McKay	D.D. McKay
W.F. MacKinnon	W.F. MacKinnon
John M. Robinson	John M. Robinson
Elliott Spafford	Elliott Spafford
J.A. MacMurray, Ex-officio	J.A. MacMurray, Ex-officio

WESTERN DISTRICT

W.M. Reay, Chairman	W.M. Reay, Chairman
J.P. O'Brien, Vice-Chairman	J.P. O'Brien, Vice-Chairman
J.M. MacKinnon	J.M. MacKinnon
J.G. MacKinnon & Co.	J.G. MacKinnon & Co.



THE I.D.A.C. - EXHIBIT D

PAGE 4

D. Dlouhy	La Maison Bienvenu LimiteeMontreal
G. Falardeau	J.T. Gendron Inc....Quebec City
L. Heslop	Bell, Gouinlock & Company, Limited...Montreal.
L.P. Letarte	La Corporation de Prets de QuebecQuebec City
R.W. MacKeen	Greenshields IncorporatedMontreal
W.G. Pavey	W.C. Pitfield & Company Limited....Montreal
W.A. Stewart	Midland Securities Corpn. Limited....Montreal
J. Edgar Hill, Ex-officio	Royal Securities Corporation Limited....Montreal.
<u>ONTARIO DISTRICT</u>	
D.S. Beatty, Chairman	Burns Bros. & Denton Limited...Toronto
D.R. Annett, Vice-Chairman	Annett & Company Limited... Toronto
Philip J. Chadsey	Wood, Gundy & Company Limited...Toronto
M.D. Cox	Anderson & Company Limited ...Toronto
Robert W. Gouinlock, Jr.	Bell, Gouinlock & Company, Limited....Toronto.
J. Ross Hilborn	McLeod, Young, Weir & Company Limited...Toronto
William N. Hovey	Equitable Securities Canada Limited...Toronto
E.P. Jarvis	Wisener, Mackellar and Company Limited...Toronto
L.E. Mayhew	Harris & Partners LimitedToronto
J.D. Schultz	Dominion Securities Corporation Limited...Toronto



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THE I.D.A.C. -- EXHIBIT D

PAGE 5

C.R. Slipp	Wills, Bickle & Company Limited...Toronto
D.I. Webb	Merrill Lynch, Pierce, Fenner & Smith Incorporated.... Toronto
D.B. Shaw, Ex-officio	A.E. Ames & Co. Limited ...Toronto
A.J. Milner, Ex-officio	Mills, Spence & Co. LimitedToronto
Roy W. Hardaker, Ex-officio	Cochran, Murray & Co. LimitedHamilton
C.E. Medland, Ex-officio	Wood, Gundy & Company LimitedKitchener
R.A. MacDonald, Ex-officio	A.E. Ames & Co. Limited... London
V.S. Castledine, Ex-officio	V.S. Castledine & Company Limited....Ottawa.

MID-WESTERN DISTRICT

D.J. Langill, Chairman	W.C. Pitfield & Company, Limited...Winnipeg
J.D. Blyth	Royal Securities Corporation Limited....Winnipeg
M.J. Bulford	Greenshields Incorporated.... Winnipeg
W. Lyle Dyker, Secretary	Osler, Hammond & Nanton Limited...Winnipeg
W.E. Heaver	Nesbitt, Thomson and Company, Limited...Regina
John Graham, Jr.	Bell, Gouinlock & Company, Limited...Winnipeg
W.A. Kinch	Dominion Securities Corporation Limited..Winnipeg
A.K. McCord	A.E. Ames & Co. LimitedWinnipeg
J.A. MacKnight	James Richardson & SonsWinnipeg
W.S. Dunlop, Ex-officio	Oldfield, Kirby & Gardner Limited...Winnipeg



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THE C.P.A. - EXHIBIT B

Wills, Bickie & Company Limited... Toronto	C.B. Slipp
Smith & Smith Incorporated... Toronto	D.L. Webb
A.E. Ames & Co. Limited... Toronto	D.B. Shaw, Ex-officio
Mills, Spence & Co. Limited... Toronto	A.J. Milner, Ex-officio
Wood, Gundy & Company Limited... Hamilton	W.W. Hargrave, Ex-officio
A.E. Ames & Co. Limited... London	C.E. Neiland, Ex-officio
V.S. Castledine & Company Limited... London	A.A. MacDonald, Ex-officio
W.L. Parnell & Company Limited... Winnipeg	V.E. Gaslingham, Ex-officio

WID-EXHIBIT B

Royal Securities Corporation Limited... Winnipeg	J.D. Blyth
Winnipeg	M.J. Bulford
Winnipeg	W. Lyle Dyker, Secretary
Winnipeg	W.H. Harvey
Winnipeg	John Wilson, Jr.
Winnipeg	A.A. Kinch
Winnipeg	A.E. McGord
Winnipeg	J.A. MacKnight
Winnipeg	A.J. Dunlop, Ex-officio



THE I.D.A.C. - EXHIBIT D

PAGE 6

ALBERTA DISTRICT

K.M. Johnston, Chairman	Wood, Gundy & Company Limited....Calgary
O.E. Buker	James Richardson & SonsCalgary
R. Copithorn	W.C. Pitfield & Company, Limited...Edmonton
Dennis Bessex	Nesbitt, Thomson and Company, Limited...Calgary
Lloyd J. Knowler	Osler, Hammond & Nanton Limited..Edmonton
Harold MacKeen	Toole, Peet Investments, Limited...Calgary
William Mathewson	McLeod, Young, Weir & Company Limited...Calgary
R. Montague	Dominion Securities (Alberta) Limited..Edmonton
Howard Ritchie	Sydie, Sutherland & Ritchie Ltd....Edmonton
T.W. Meredith, Ex-officio	Osler, Hammond & Nanton Limited...Calgary

PACIFIC DISTRICT

Ross Wilson, Chairman	A.E. Ames & Co. Limited ...Vancouver
A.H. Cater, Vice-Chairman	Royal Securities Corporation Limited...Vancouver
H.H. Dingle	Wood, Gundy & Company Limited...Vancouver
J.H. Lamprey	Yorkshire Securities Limited....Vancouver
G.H. Nation	Dominion Securities Corporation LimitedVancouver
H.B. Paterson	Norman R. Whittall LimitedVancouver
T.B. Read	Thomas B. Read Company Ltd.Vancouver



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ALBERTA DISTRICT

Wood, Gundy & Company
(Limited) ...

W.K. ...

James Richardson & Sons

C.E. Baker

W.C. Pittfield & Company
(Limited) ...

A. Gopichorn

Nesbitt, Thomson and
Company, Limited ... Calgary

...

Oster, Hammond & Hendon
(Limited) ...

Eric J. Knowler

Tools, Best Investments,
Limited ... Calgary

...

Company Limited ... Calgary

William Mathewson

(Limited) ...

...

Sydie, Sutherland & Ritchie
(Limited) ...

...

... (Limited) ...

...

ALBERTA DISTRICT

A.E. Ames & Co. Limited
... Vancouver

...

... (Limited) ...

A.H. Carter, Vice-Chairman

Wood, Gundy & Company
(Limited) ... Vancouver

H.H. Dingle

... (Limited) ...

J.H. Larpney

... (Limited) ...

G.H. Nation

Norman R. Whitford Limited
... Vancouver

H.B. Paterson

... (Limited) ... Vancouver

...



THE I.D.A.C. - EXHIBIT D

PAGE 7

K.G. Russell	McLeod, Young, Weir & Company Limited...Vancouver
J.E. Smart	Pemberton Securities Limited, ...Vancouver
L.B. Williams	Hagar Investments Ltd.... Victoria
W. Tom Brown, Ex-officio	Odlum Brown Investments Ltd.Vancouver

NATIONAL BUSINESS CONDUCT COMMITTEE

Eric S. Morse, Chairman	W.C. Pitfield & Company, Limited....Montreal
Norman J. Alexander	James Richardson & Sons.... Winnipeg
E.H. Ely	Wood, Gundy & Company LimitedToronto
R.H. Dean	Nesbitt, Thomson and Company, Limited....Montreal
N.H. Gunn	Bell, Gouinlock & Company, Limited....Toronto

DISTRICT BUSINESS CONDUCT COMMITTEES

ATLANTIC DISTRICT

J.W. Ritchie, Chairman	Eastern Securities Company Limited...Halifax
J.A. MacMurray	Eastern Securities Company Limited....Saint John
R.C. Hebb	Dominion Securities Corporation Limited...Halifax
F.J. Brennan	F.J. Brennan & Company Limited...Saint John
G.W. Ramsay	Stanbury & Company LimitedSaint John
J.D. Wood	Nesbitt, Thomson and Company, Limited....Halifax
H.L. Gassard, Ex-officio	The Investment Dealers' Association of Canada..... Toronto



1935

1935

1935

1935

McLeod, Young, Weir & Company Limited...Vancouver	
Pemberton Securities Limited, ...Vancouver	
Hagan Investments Ltd...	L.B. Williams
W. Tom Brown, Ex-officio	

NATIONAL BUSINESS COUNCIL

James Richardson & Sons... Winnipeg	Eric S. Morse, Chairman
Wood, Gundy & Company Limited ...Toronto	E.H. Rix
Nesbitt, Thomson and Company, Limited, Toronto	H.E. Dean
Bell, Gouinlock & Company, Limited, Toronto	M.H. Carr

ATLANTIC DISTRICT

Atlantic Maritime Limited...Halifax	J.W. Ritchie, Chairman
Atlantic Maritime Limited...Halifax	J.A. Macdonald
Atlantic Maritime Limited...Halifax	R.C. Webb
F.J. Brennan & Company Limited...Halifax	F.J. Brennan
Standbury & Company Limited ...Halifax	G.W. Ramsey
Standbury & Company Limited ...Halifax	F.D. Wood
Association of Canada...	H. Gassard, Ex-officio



THE I.D.A.C. - EXHIBIT D

PAGE 8

QUEBEC DISTRICT

W.M. Reay, Chairman	Nesbitt, Thomson and Company, Limited...Montreal
J. Edgar Hill	Royal Securities Corporation Limited...Montreal
R.B. Casgrain	Casgrain & Company LimitedMontreal
Andrew S. Beaubien	L.G. Beaubien & Co.LimitedMontreal
Dudley Dawson	Greenshields IncorporatedMontreal
E.F.C. Kinnear	W.C. Pitfield & Company, Limited....Montreal
H.L. Gassard, Ex-officio	The Investment Dealers' Association of CanadaToronto

ONTARIO DISTRICT

D.S. Beatty, Chairman	Burns Bros. & Denton Limited....Toronto
D. Bruce Shaw	A.E. Ames & Co. LimitedToronto
R.A. Daly, Jr.	R.A. Daly & Company LimitedToronto
Frank D. Lace	Matthews & Company LimitedToronto
R.K. Wright	Mills, Spence & Co.Limited ...Toronto
M.F. Newman	Cochran, Murray & Co. Limited...Toronto
H.L. Gassard, Ex-officio	The Investment Dealers' Association of CanadaToronto

MID-WESTERN DISTRICT

D.J. Langill, Chairman	W.C. Pitfield & Company Limited...Winnipeg
W.S. Dunlop	Oldfield, Kirby & Gardner Limited...Winnipeg
J.D. Bulgin	Dominion Securities Corporation Limited..Winnipeg

QUEBEC DISTRICT

W.M. Reay, Chairman	Messitt, Thomson and Company, Limited, Montreal
J. Edgar Hill	Royal Insurance Corporation Limited, Montreal
R.B. Gasparin	Gasparin & Company Limited ...Montreal
Andrew S. Beaubien	L.G. Beaubien & Co. Limited ...Montreal
Budley Dawson	Greenhields Incorporated ...Montreal
H.R.C. Kinnear	V.C. Patterson & Company Limited, Montreal
H.L. Gassard, Ex-officio	The Investment Dealers Association of Canada ...Toronto

ONTARIO DISTRICT

D.S. Beatty, Chairman	Beatty, Beatty & Company Limited, Toronto
D. Bruce Shaw	A.Z. Ames & Co. Limited ...Toronto
H.A. Dwyer, Jr.	R.A. Daly & Company Limited ...Toronto
Frank M. East	Matthews & Company Limited ...Toronto
A.E. Wright	Miller, Spence & Co. Limited ...Toronto
M.R. Newman	Coehman, Murray & Co. Limited, Toronto
H.L. Gassard, Ex-officio	The Investment Dealers Association of Canada ...Toronto

NEW-YORK DISTRICT

D.J. Langill, Chairman	W.C. Pluffield & Company Limited, New York
W.S. Dunlop	Oldfield, Kirby & Gardner Limited, New York
J.D. Bulfinch	Bulfinch & Company Limited, New York



THE I.D.A.C. - EXHIBIT D PAGE 9

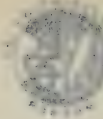
Kenneth Rothwell	A.E. Ames & Co. LimitedWinnipeg
Charles McKelvie	James Richardson & SonsWinnipeg
G.S. Swindell	Wood, Gundy & Company Limited...Winnipeg
H.L. Gassard, Ec-officio	The Investment Dealers' Association of CanadaToronto

ALBERTA DISTRICT

K.M. Johnston, Chairman	Wood, Gundy & Company Limited...Calgary
T.W. Meredith	Osler, Hammond & Nanton Limited...Calgary
A.H. Turney	Locke, Gray & Company Limited...Calgary
W.V. Warner	James Richardson & Sons ...Edmonton
W.R. Taprell	Carlile & McCarthy Ltd.... Calgary
H.R. Farnsworth	Burns Bros. & Denton Limited...Calgary
H.L. Gassard, Ex-officio	The Investment Dealers' Association of Canada... Toronto

PACIFIC DISTRICT

Ross Wilson, Chairman	A.E. Ames & Co. Limited ...Vancouver
W.T. Brown	Odum Brown Investments Ltd....Vancouver
A.G. Osburn	Pemberton Securities Limited...Vancouver
J.M. McAvity	W.C. Pitfield & Company Limited...Vancouver
J. Denis Hagar	Hagar Investments Ltd.... Victoria
G.D. Sherwood	Thomas B. Read Company Ltd...Vancouver



Wales, Dominion of
1914

Wales, Dominion of
1914

TABLE 2

THE D.O.W. - EXHIBIT D

A.R. Ames & Co. Limited
....Winnipeg

Winnipeg, Manitoba

James Richardson & Sons
....Winnipeg

Winnipeg, Manitoba

Wood, Gundy & Company
Limited, Winnipeg

Winnipeg, Manitoba

The Investment Dealers'
Association of Canada
....Toronto

Toronto, Ontario

ALBERTA DISTRICT

Wood, Gundy & Company
Limited...Calgary

Calgary, Alberta

Oster, Hammond & Norton
Limited...Calgary

Calgary, Alberta

Locke, Gray & Company
Limited, Calgary

Calgary, Alberta

James Richardson & Sons
....Calgary

Calgary, Alberta

Garfield & McCarthy Ltd....
Calgary

Calgary, Alberta

Burns Bros. & Denton
Limited...Calgary

Calgary, Alberta

The Investment Dealers'
Association of Canada...
Toronto

Toronto, Ontario

PATRIC DISTRICT

A.R. Ames & Co. Limited
...Vancouver

Vancouver, British Columbia

W.T. Brown
Ltd....Vancouver

Vancouver, British Columbia

W.C. Pittfield & Company
Limited...Vancouver

Vancouver, British Columbia

W.C. Pittfield & Company
Limited...Vancouver

Vancouver, British Columbia

W.C. Pittfield & Company
Limited...Victoria

Victoria, British Columbia

Thomas B. Read Company
Ltd....Vancouver

Vancouver, British Columbia



H.L. Gassard, Ex-officio The Investment Dealers'
Association of Canada
....Toronto

DISTRICT ASSOCIATION AUDITORS

Lee & Martin Maritime Life Bldg. Halifax, NS 3-1311

Peat, Marwick,
Mitchell & Co. 901 Victoria Square Montreal UN6-2693

Clarkson, Gordon
& Co. 15 Wellington St.W. Toronto, Ont EM8-2751

Deloitte, Plender,
Haskins & Sells 60 Osborne St.N. Winnipeg, SP4-1601

Peat, Marwick,
Mitchell & Co. 508-309 8th Ave.W. Calgary AM6-6041

Buttar & Chiene 789 West Pender St. Vancouver MU3-6964

PAST PRESIDENTS

1916-1917 *William Hanson Hanson Bros. Montreal

1917-1918 *A.E. Ames A.E. Ames & Co.Ltd. Toronto

1918-1919 *J.M. Mackie C. Meredith & Co. Montreal

1919-1920 *Sir Augustus
Nanton Osler, Hammond &
Nanton Ltd. Winnipeg

1920-1921 *J.H. Gundy Wood, Gundy & Co. Toronto

1921-1922 *R.D. Bell Greenshields & Co. Montreal

1922-1923 #A.L. Crossin Oldfield, Kirby &
Gardner Limited Winnipeg

1923-1924 *J.W. Mitchell Dominion Securities
Corporation Ltd. Toronto

1924-1925 *J.A. Eccles Harris, Forbes & Co. Montreal

1925-1926 *L.W. Hicks L.W. Hicks & Co. Winnipeg

1926-1927 R.A. Daly R.A. Daly Co.Ltd. Toronto

1927-1928 *E.G. Hanson Hanson Bros. Montreal

1928-1929 *Harry Ford Osler, Hammond &
Nanton Ltd. Winnipeg

1929-1930 *F.J. Coombs A.E. Ames & Co. Ltd. Toronto

1930-1931 *N.S. Brooke Royal Securities
Corporation Ltd. Montreal



H.L. Gossard, 24-01110
Association of Canada
Toronto

DISTRICT ASSOCIATION AUDITORS

Lee & Martin	Maritime Life Bldg. Halifax NS	3-1311
Best, Marwick, Mitchell & Co.	501 Victoria Square Montreal	110-2511
Clarkson, Gordon & Co.	15 Wellington St. W. Toronto	Ont BMS-2751
Haskins & Selie	60 Osborne St. N. Winnipeg	274-1601
Best, Marwick, Mitchell & Co.	508-309 8th Ave. W. Calgary	AMS-6041
Butter & Chene	789 West Bender St. Vancouver	W13-6964

PAST PRESIDENTS

1917-1918	*A.E. Ames	A.E. Ames & Co. Ltd. Toronto
1918-1919	*J.H. Gundy	Wood, Gundy & Co. Toronto
1919-1920	*R.D. Bell	Greenshields & Co. Montreal
1920-1921	*A.L. Crossin	Oldfield, Kirby & Gardner Limited Winnipeg
1921-1922	*F.J. Gomba	A.E. Ames & Co. Ltd. Toronto
1922-1923	*H.G. Hanson	Hanson Bros. Montreal
1923-1924	*H.W. Hicks	L.W. Hicks & Co. Winnipeg
1924-1925	*R.A. Daly	R.A. Daly Co. Ltd. Toronto
1925-1926	*H.W. Hicks	L.W. Hicks & Co. Winnipeg
1926-1927	*H.W. Hicks	L.W. Hicks & Co. Winnipeg
1927-1928	*H.W. Hicks	L.W. Hicks & Co. Winnipeg
1928-1929	*H.W. Hicks	L.W. Hicks & Co. Winnipeg
1929-1930	*H.W. Hicks	L.W. Hicks & Co. Winnipeg



	<u>THE I.D.A.C. - EXHIBIT D</u>		<u>PAGE 11</u>
1			
2	1931-1932	*A.H. Williamson	Wood, Gundy & Co. Vancouver
3	1932-1933	J.G. Weir	McLeod, Young, Weir & Company Toronto
4	1933-1934	*W.C. Pitfield	W.C. Pitfield & Company Ltd. Montreal
5			
6	1934-1935	R.W. Gouinlock	Bell, Gouinlock & Co. Limited Toronto
7			
8	1935-1936	J. Ernest Savard	Savard, Hodgson & Co. Inc. Montreal
9	1936-1937	*R.D. Baker	James Richardson & Sons Winnipeg
10			
11	1937-1938	#K.M. Pringle	Dominion Securities Corporation Ltd. Toronto
12	1938-1939	D.K. Baldwin	Nesbitt, Thomson & Co. Ltd. Montreal
13			
14	1939-1940	W.P. Scott	Wood, Gundy & Co. Toronto
15	June 1940- Nov. 1940	#E.C. Cumberland	Hanson Bros. Montreal
16	Nov. 1940- Nov. 1941	*S.B. Hammond	Royal Securities Corporation Ltd. Montreal
17			
18	Nov. 1941-1942		
19	June 1943	H.E. Cochran	Cochran, Murray & Co. Limited Toronto
20	1943-1944	W.T.K. Collier	Collier, Norris & Quinlan Ltd. Montreal
21			
22	1944-1945	*A.G.A. Spence	Mills, Spence & Co. Toronto
23	1945-1947	A.S. Torrey	W.C. Pitfield & Co. Montreal
24	1947-1948	J.A. Gairdner	Gairdner & Co. Ltd. Toronto
25	1948-1949	G.G. Ryan	L.G. Beaubien & Co. Limited Montreal
26	1949-1950	#J.B. Ridley	A.E. Ames & Co. Toronto
27	1950-1951	Peter Kilburn	Greenshields & Co. Inc. Montreal
28			
29	1951-1952	W.J. Borrie	Pemberton Securities Ltd. Vancouver
30			



THE I.D.A.C. - EXHIBIT D PAGE 12

1952-1953	H.S. Backus	McLeod, Young, Weir & Co. Limited	Toronto
1953-1954	Gerard Gingras	Rene-T. Leclerc, Incorporee	Montreal
1954-1955	J.R. Hughes	Royal Securities Corporation Ltd.	Montreal
1956-1957	N.H. Gunn	Bell, Gouinlock & Company, Limited	Toronto
1957-1958	R.H. Dean	Nesbitt, Thomson & Company, Limited	Montreal
1958-1959	E.H. Ely	Wood, Gundy & Co. Limited	Toronto
1959-1960	N.J. Alexander	James Richardson & Sons	Winnipeg
1960-1961	Eric S. Morse	W.C. Pitfield & Co.	Montreal

* Deceased

Retired



A. 100
- 4 -

100-1000
100-1000

THE J.D.A. - EXHIBIT D PAGE 12

1953-1953	J.D. Baines	John D. Baines & Co. Limited	Toronto
1953-1954	Gerard Gintars	Gerard Gintars	Toronto
1954-1955	J.R. Hughes	John R. Hughes Corporation Ltd.	Toronto
1956-1957	N.H. Gunn	N.H. Gunn & Son, Limited	Toronto
1957-1957	R.H. Dean	R.H. Dean & Company, Limited	Toronto
1958-1959	E.H. Ely	Wood, Gundy & Co. Limited	Toronto
1959-1960	H.J. Alexander	James Richardson & Sons	Winnipeg
1960-1961	Eric S. Morse	Eric S. Morse	Winnipeg

* Deceased

Retired



THE I.D.A.C. - EXHIBIT G

CUMULATIVE RECORD OF COURSE RESULTS

Cumulative Record of New Enrollments from our Members and Passes (Excluding Readership and Other Enrollments)

COURSE 1

Jan. 1948 - June, 1948	Enrolled	315	Completed	262
Jan. 1949 - June, 1949	"	42	"	33
Apr. 1950 - Dec., 1950	"	104	"	64
Jan. 1951 - June, 1951	"	137	"	93
Sept. 1951 - Mar., 1952	"	137	"	74
Sept. 1952 - June, 1953	"	292	"	169
Sept. 1953 - June, 1954	"	222	"	111
Sept. 1954 - June, 1955	"	278	"	160
Sept. 1955 - June, 1956	"	426	"	163
Sept. 1956 - June, 1957	"	413	"	242
Sept. 1957 - June, 1958	"	495	"	285
Sept. 1958 - June, 1959	"	301	"	189
Sept. 1959 - June, 1960	"	439	"	254
Sept. 1960 - June, 1961	"	266	"	175

3,867 2,274

COURSE II

Dec. 1948 - Feb., 1950	Enrolled	361	Completed	159
Apr. 1950 - Mar., 1951	"	41	"	19
May, 1951 - Apr., 1952	"	113	"	55
Sept. 1952 - June, 1953	"	167	"	95
Sept. 1953 - June, 1954	"	159	"	77
Sept. 1954 - June, 1955	"	148	"	92
Sept. 1955 - June, 1956	"	190	"	103
Sept. 1956 - June, 1957	"	183	"	134
Sept. 1957 - June, 1958	"	166	"	125
Sept. 1958 - June, 1959	"	218	"	176
Sept. 1959 - June, 1960	"	175	"	131
Sept. 1960 - June, 1961	"	208	"	161

2,129 1,327

Grand Total Enrollment Grand Total
both courses 5,996 Completed 3,601

Percentage Completions

To June 1961 - 58.9 per cent of Course I students and 62.3 per cent of Course II students who enrolled completed the Course. In June 1961, the latest year available, 65.7 per cent of Course I students and 77.4 per cent of Course II students completed.

EXHIBIT C - 1961

CUMULATIVE RECORD OF COURSE RESULTS

Cumulative Record of New Enrollments from our Members and Passes (Excluding Readership and Other Enrollments)

COURSE I			
Enrolled	Completed		
1948 - June, 1948	315	1048	Jan.
" " " " " "	45	1049	Jan.
" " " " " "	104	1050	Apr.
" " " " " "	137	1051	Jan.
" " " " " "	137	1052	Sept.
" " " " " "	292	1053	Sept.
" " " " " "	292	1054	Sept.
" " " " " "	278	1055	Sept.
" " " " " "	426	1056	Sept.
" " " " " "	413	1057	Sept.
" " " " " "	495	1058	Sept.
" " " " " "	301	1059	Sept.
" " " " " "	439	1060	Sept.
" " " " " "	266	1061	Sept.
	3,867		

COURSE II			
Enrolled	Completed		
1948 - Feb., 1950	361	1048	Dec.
" " " " " "	41	1050	Apr.
" " " " " "	113	1051	May
" " " " " "	167	1052	Sept.
" " " " " "	159	1053	Sept.
" " " " " "	148	1054	Sept.
" " " " " "	190	1055	Sept.
" " " " " "	183	1056	Sept.
" " " " " "	166	1057	Sept.
" " " " " "	218	1058	Sept.
" " " " " "	175	1059	Sept.
" " " " " "	208	1060	Sept.
	2,129		

Grand Total Enrollment 3,601 Completed 3,601

Percentage Completions

To June 1961 - 58.9 per cent of Course I students and 62.3 per cent of Course II students who enrolled completed the course. In June 1961, the latest year available, 65.7 per cent of Course I students and 77.4 per cent of Course II students completed.



PART II - I.D.A.C. - EXHIBIT H

I.D.A.C. Adult Lecture Courses on "Understanding Investment Securities" - Fall, 1961 to Spring, 1962. Each course consisted of between 5 and 15 evening lectures.

Kitsilano High School, Vancouver, B.C.	93
Burnaby Public School, Burnaby, B.C.	17
Vancouver Technical School, Vancouver, B.C.	64
University of British Columbia, Vancouver, B.C.	153
University of Alberta, Edmonton, Alberta	75
University of Alberta, Calgary, Alberta	70
Regina Public School Board, Regina, Saskatchewan	44
University of Manitoba, Winnipeg, Manitoba	148
University of Toronto, Toronto, Ontario	80
Recreation Commission, Village of Forest Hill, Ont.	60
Recreation Commission, Leaside, Ontario	50
Young Men's Canadian Club, Toronto, Ont.	35
MacLean-Hunter Publishing Co.Ltd., Toronto, Ont.	110
Marsh & McLennan Ltd., Toronto, Ont.	50
Y.M.C.A. Adult Education Programme, Hamilton, Ont.	38
St. Catharines Public School Board, St.Catharines	25
Ottawa Public School Board, Ottawa, Ont.	50
University of Montreal, Montreal, P.Q.	152
McGill University, Montreal, P.Q.	255
University of Laval, Quebec, P.Q.	72
Bank of Montreal, Montreal, P.Q.	103
Saint Mary's University, St. John, N.B.	60

Total 1804



PART II - I.D.A.C. - EXHIBIT H

I.D.A.C. Public Inquiry Committee on Investment
Investment Securities" - Fall, 1961 to Spring, 1962.
This report contains the findings of the Committee.

- 93 Kitaleano High School, Vancouver, B.C.
- 94 St. Mary's Public School, Vancouver, B.C.
- 95 Vancouver Technical School, Vancouver, B.C.
- 96 University of British Columbia, Vancouver, B.C.
- 97 University of Alberta, Edmonton, Alberta
- 98 University of Alberta, Calgary, Alberta
- 99 Regina Public School Board, Regina, Saskatchewan
- 100 University of Manitoba, Winnipeg, Manitoba
- 101 University of Toronto, Toronto, Ontario
- 102 Recreation Commission, Village of Forest Hill, Ont.
- 103 Recreation Commission, Leaside, Ontario
- 104 Young Men's Canadian Club, Toronto, Ont.
- 105 MacLean-Hunter Publishing Co. Ltd., Toronto, Ont.
- 106 Marsh & McLennan Ltd., Toronto, Ont.
- 107 Y.M.C.A. Adult Education Programme, Hamilton, Ont.
- 108 St. Catharines Public School Board, St. Catharines
- 109 St. Catharines Public School Board, St. Catharines
- 110 University of Montreal, Montreal, P.Q.
- 111 McGill University, Montreal, P.Q.
- 112 University of Laval, Quebec, P.Q.
- 113 Bank of Montreal, Montreal, P.Q.
- 114 St. Mary's Public School Board, St. Mary's, N.B.



Nethercut & Young

Toronto, Ontario

A.164

- B -

BRIEF TO THE ROYAL COMMISSION ON BANKING AND FINANCE

APPENDIX B

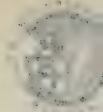
The Finance Department
and

Federal and Provincial Government Financing

Submitted by
THE INVESTMENT DEALERS' ASSOCIATION OF CANADA

I N D E X

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11	Monetary Policy	A.171
12	The Bank Rate	A.172
13	Overall Government Policy	A.173
14	Comments on the Federal Debt	A.174
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REPORT TO THE ROYAL COMMISSION ON FINANCE AND FINANCING

APPENDIX B

The Finance Department
and
Federal and Provincial Government Financing

Submitted by
THE INVESTMENT DEALERS' ASSOCIATION OF CANADA

I N D E X

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A.171	Monetary Policy
A.172	The Bank Rate
A.173	Overall Government Policy
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A.175	Marketing of New Issues and Investor Attitudes
A.176	Investor Attitudes
A.178	Recommendation
A.179	Federal and Provincial Financing in the Last Ten Years Under Review
A.180	Recommendations
A.181	Comparison Between Canada and the United Kingdom
A.182	Recommendations
A.183	Comparison Between Canada and the United States
A.184	Recommendations
A.185	Recommendations
A.186	Government of Canada Issues
A.187	Recommendations on Government Financing
A.188	Recommendations on C.N.R. Financing
A.189	Provincial Financing
A.190	Method of Distributing Provincial Securities to the Public



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1 BRIEF TO THE ROYAL COMMISSION ON BANKING AND
2 FINANCE

3 1. We have been invited to present a Brief to the
4 Royal Commission on Banking and Finance. This portion
5 of the Brief covers The Finance Department and Federal
6 and Provincial Government Financing.

7 2. Within the framework of our particular subject
8 and in accordance with the terms of reference, we will
9 comment on The Finance Department, the investor who
10 provides capital to the Federal and Provincial Governments
11 and those who use it, the dealer who mobilizes capital
12 and those legislative, functional and other influences
13 which set the climate in which the users of capital and
14 financial intermediaries operate. Our comments will be
15 confined to the postwar period for two reasons:

16 (a) The second World War brought about
17 such great changes in the Canadian
18 debt structure and debt management
19 that any study of conditions as they
20 existed during the War or in the
21 prewar period would have very little
22 bearing on the subject now.

23 (b) The inflationary tendencies brought
24 about by World War II and continuing
25 through the postwar period have
26 brought about fundamental changes
27 in investor attitudes and decisions.

28 3. In the early years after the War, as a result
29 of high taxation, increased living costs and continuous
30 inflation, the investor became aware of the advisability

BRIEF TO THE ROYAL COMMISSION ON BANKING AND
FINANCE

1. We have been invited to present a Brief to the Royal Commission on Banking and Finance. This portion of the Brief covers The Finance Department and Federal and Provincial Government financing.

2. Within the framework of our particular subject and in accordance with the terms of reference, we will comment on The Finance Department, the investor who

provides capital to the Federal and Provincial Governments and those who use it, the dealer who mobilizes capital and those legislative, functional and other influences which set the climate in which the users of capital and financial intermediaries operate. Our comments will be confined to the postwar period for two reasons:

(a) The second World War brought about such great changes in the Canadian debt structure and debt management that any study of conditions as they existed during the War or in the prewar period would have very little bearing on the subject now.

(b) The inflationary tendencies brought about by World War II and continuing through the postwar period have brought about fundamental changes in investor attitudes and decisions.

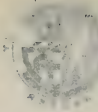
3. In the early years after the War, as a result of high taxation, increased living costs and continuous inflation, the investor became aware of the advisability



1 of having at least a portion of his money in securities
2 giving him some protection against the continuous erosion
3 in the value of the dollar. At the same time, he
4 became aware that a new era of economic expansion was
5 commencing and wished to share to the utmost in the
6 economic growth of the country. This led the investor
7 to put more of his worth into the shares of Canadian
8 corporations and this tendency has been encouraged by
9 Government policy through the introduction of the
10 "dividend tax credit", which now stands at 20 per cent,
11 as a means of fostering greater development and ownership
12 of Canadian industry by Canadians.

13 4. The central weakness of the postwar years,
14 insofar as the value of fixed income securities was
15 concerned, was the result of the inflationary forces
16 created during the War. The pent-up demand for all forms
17 of consumer goods and social requirements such as housing,
18 schools, highways, hospitals, etc., coupled with the
19 development of new products and the world demand for our
20 raw materials and semi-finished and finished products
21 created a demand for labour, materials and capital of
22 unprecedented size. The demand for labour was eased by
23 returning veterans and an aggressive immigration policy.
24 The demand for capital during the postwar period of
25 expansion was satisfied by generation of new money through
26 the buoyancy of the Canadian economy and importation of
27 capital from abroad with an accelerated tendency towards
28 importations of massive amounts during the period 1956
29 to 1961.

30 5. In the process institutions, other than banks



of having at least a portion of his money in securities giving him some protection against the continuous erosion in the value of the dollar. At the same time, he became aware that a new era of economic expansion was commencing and wished to share to the utmost in the economic growth of the country. This led the investor to put more of his worth into the shares of Canadian corporations and this tendency has been encouraged by Government policy through the introduction of the "dividend tax credit", which now stands at 20 per cent, as a means of fostering greater development and ownership of Canadian industry by Canadians.

4. The central weakness of the postwar years, insofar as the value of fixed income securities was concerned, was the result of the inflationary forces created during the war. The pent-up demand for all forms of consumer goods and social expenditures such as housing, schools, highways, hospitals, etc., coupled with the development of new products and the world demand for raw materials and semi-finished and finished products created a demand for labour, materials and capital of unprecedented size. The demand for labour was eased by returning veterans and an aggressive immigration policy. The demand for capital during the postwar period of expansion was satisfied by generation of new money through the buoyancy of the Canadian economy and importation of capital from abroad with an accelerated tendency towards importations of massive amounts during the period 1955 to 1961.

5. In the process institutions, other than banks



1 and the general public, reduced the proportion of Federal
2 Government bonds in their portfolios, not only through
3 committing most newly acquired funds to investment in
4 higher yielding obligations of provinces, municipalities
5 and corporations as well as mortgages, but by selling
6 holdings of Victory Bonds. These Victory Bonds were
7 then retired by the Government through budgetary
8 surpluses or acquired by the banking system where the
9 acquisition resulted in the monetization of the equivalent
10 portion of the national debt to the extent that the
11 increase in the money supply exceeded the development of
12 the economy.

13 6. During most of the postwar period, the
14 Federal Government, by retaining by agreement or otherwise
15 the main sources of taxation, operated with surpluses
16 and the burden of finding new capital for expansion fell,
17 for the most part, on the provinces, municipalities and
18 private industry.

19 7. In the same period the Canadian dollar lost
20 approximately 40 per cent of its purchasing value and to
21 this extent, the investor who bought and retained fixed
22 income securities of the Federal or Provincial govern-
23 ments was the loser. On the other hand, the investor
24 who purchased the shares of a cross-section of leading
25 Canadian corporations gained substantially due to the
26 growth in capital value of his share portfolio.

27 8. As a result, there has been and is now
28 a growing reluctance on the part of many investors to
29 put other than a limited proportion of their funds into
30 long-term bonds and unless inflationary tendencies are



and the general public, reduced the proportion of Federal Government bonds in their portfolios, not only through committing most newly acquired funds to investment in higher yielding obligations of provinces, municipalities and corporations as well as mortgages, but by selling a large amount of Federal bonds. These Federal bonds were then retired by the Government through budgetary surpluses or acquired by the banking system where the acquisition resulted in the monetization of the equivalent portion of the national debt to the extent that the increase in the money supply exceeded the development of the economy.

6. During most of the postwar period, the Federal Government, by retaining by agreement or otherwise the main source of taxation, operated with increased and the burden of finding new capital for expansion fell for the most part, on the provinces, municipalities and private industry.

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8. As a result, there has been and is now a growing reluctance on the part of many investors to put other than a limited proportion of their funds into



checked this proportion is bound to decline.

9. This was the so-called "climate" in which money was raised in Canada and "climate" is still the most powerful single factor in investment decisions at most levels today.

The Investor or Provider of Capital

10. There are, of course, important institutional groups in the Canadian economy obliged to buy fixed income securities. Most important among these are insurance companies, banks, trust companies and pension funds, who buy fixed term dollar obligations to offset fixed term dollar liabilities. However, the pension funds to a greater degree than ever before are putting a larger percentage of their investable funds into the shares of Canadian corporations as an offset to the possible further decline of the buying power of the dollar.

11. There is still a segment of the public who buy fixed term obligations of the Federal and Provincial governments, as an adjunct to an equity portfolio for the purpose of providing a liquid reserve of cash with a market value at or near cost. However, for various reasons, there does seem to be a trend away from investment in long-term Government bonds by these private investors and Canada Savings Bonds have been substituted in most of these portfolios to the extent permitted.

12. Many corporations with strong working capital positions have money available for short periods of time. This money, to a great extent, is now being invested in

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12. Many corporations with strong working capital



1 short-term Federal Government securities. A good
2 portion also is invested in other short-term debt
3 instruments, but short-term Federal Government securities,
4 because of their high degree of liquidity, are by far the
5 largest element in this sector.

6 Fiscal Policies

7 13. The fiscal policies of the Federal and
8 Provincial governments have a great bearing on the
9 attitude of the investor. In the latter part of the
10 period under review, the Federal Government accepted the
11 principles of deficit financing as a stimulus to a lagging
12 national economy, but recently proper weight does not
13 seem to have been given to the corollary of surpluses
14 and debt retirement in periods of prosperity. What tends
15 to happen is that in periods of surpluses new government
16 spending programmes are initiated in preference to debt
17 retirement. If a proper approach was taken and it was
18 coupled with a fixed annual sinking fund of 1 per cent
19 per annum on all outstanding Federal Government issues
20 over three years, a greater degree of investor confidence
21 in the security and marketability of the medium and long-
22 term bonds of the Federal Government would be generated.
23 In this connection it is pointed out that most Provinces
24 of Canada now provide sinking funds for both their direct
25 and guaranteed issues as set forth in Exhibit 1. The
26 sinking funds on Government of Canada medium and long-
27 term issues need only operate until their terms to
28 maturity are three years or less, since once an issue has
29 been less than three years to run, it becomes part of
30 the money market. It is normal policy for the central



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1 bank to operate in the money market and to purchase and
2 hold a substantial proportion of the next maturing
3 Government of Canada issue in order to provide for the
4 orderly retirement or refunding of debt. This action
5 will ensure an adequate market for three short-term
6 issues without the need of action by the sinking fund.

7 Monetary Policy

8 14. It appears to us that there is a tendency
9 for debt management policy to be unduly subordinated to
10 monetary policy and the Investment Dealers' Association
11 suggests that the Royal Commission inquire as to whether
12 debt management and control of currency have conflicting
13 interests and whether these functions should be
14 separated.

15 15. If debt management and control of
16 currency were separated and the Department of Finance
17 reassumed the direct responsibility for the management
18 of the national debt, with the exception of money market
19 securities, it would have the effect of bringing the
20 Department of Finance and the Cabinet into closer
21 association with the problems of raising money in the
22 capital markets to implement Government fiscal policies,
23 which do not now adequately seem to reflect the
24 requirements of sound debt management.

25 16. The Investment Dealers' Association also
26 believes that the Commission should inquire into the Bank
27 of Canada's role in operating the Purchase Fund and
28 trading for Government accounts to determine whether
29 these functions should be handled by the Department of
30 Finance, or other trading agencies.

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of Canada's role in operating the foreign bond and
other for government accounts in order to maintain
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(Paragraphs 17 and 18 intentionally deleted).

The Bank Rate

19. Since November 1956, the Bank Rate has been set each week at a level of $1/4$ of 1 per cent above the average rate on accepted tenders at the weekly auction of Government of Canada 3-month Treasury Bills.

20. Recently, this method of determining the Bank Rate has been the subject of a good deal of discussion and various views have been expressed. The Investment Dealers' Association feels that there is some merit in returning to the fixed Bank Rate as an instrument signalling important changes in monetary policy. If this were done, there would, of course, be a heavier penalty for chartered banks or money market dealers to using the rediscount privileges of the central bank. As far as the chartered banks are concerned, this would not be too onerous since they seldom use this privilege. However, for the money market dealers the "floating rate" has the advantage of limiting the penalty rate at which the dealers can borrow from the central bank. With a fixed Bank Rate there would be occasions when the cost of day loans would be above the running yield on Treasury Bills. At times when this occurred, dealers would be reluctant to hold large inventories and this in turn could tend to inhibit the size of the money market.

21. It therefore seems appropriate to study the possibilities of returning to an administered Bank Rate, which would clearly indicate the state of the Canadian economy, not only in relation to the internal

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1 situation in Canada, but also in relation to other major
2 countries such as Great Britain and the United States.
3 The Bank Rate would be the rate which signals important
4 changes in monetary policy. In addition, and in order
5 to continue to foster the growth of the money market, the
6 money market participants should continue to have the
7 right to sale and repurchase agreements with the Bank of
8 Canada, to the extent of their lines of credit at the
9 average tender for 90-day Bills, plus $1/4$ of 1 per cent.

10 Overall Government Policy

11 22. We believe that the Government should
12 pursue appropriate fiscal and monetary policies that have
13 as their basic objective an adequate rate of economic
14 growth which sustains a high level of productivity and
15 employment and reasonable stability of prices. In
16 addition to these objectives we believe the scope and
17 quality of monetary and fiscal measures should be in
18 keeping with the capacity of the Government to finance
19 the national debt without straining its credit resources
20 or impairing the confidence of investors at home and
21 abroad in the integrity of the Canadian dollar and debt
22 obligations of the Government of Canada. To maintain
23 confidence in Government of Canada securities we feel
24 that the authorities responsible for managing national
25 debt should reiterate their belief in the following
26 generally accepted basic principles of responsible debt
27 management -

28 (a) Government securities must be sound
29 and dependable investments.

30 (b) Extremes of inflation and deflation

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(a) Government securities must be sound

and dependable investments.

(b) Extremes of inflation and deflation



1 should be avoided.

2 (c) The National Debt should be held
3 by as great a number of individuals,
4 institutions and corporations as
5 possible.

6 (d) Fiscal policy should be directed
7 towards continuous growth in relation
8 to national income.

9 (e) Periods of budgetary deficits should
10 be offset more equitably by periods
11 of budgetary surpluses.

12 Comments on the Federal Debt

13 23. Exhibit II shows the distribution of the
14 Federal debt under four main headings. The Bank of
15 Canada, the chartered banks, Government of Canada accounts,
16 such as unemployment insurance, securities investment
17 and the general public. Exhibit III shows the Total Debt,
18 the Average Term, the Amount of Total Debt under 3 years,
19 the Percentage of the Total Debt under 3 years, the
20 Population and the Debt Per Capita as of December 31st,
21 1946, 1951, 1956 and 1961.

22 24. During the period marketable debt declined
23 from \$16,044,000,000 to \$14,575,000,000, but the amount
24 of Canada Savings Loans outstanding increased from
25 \$469,000,000 to \$4,079,000,000. Thus we are now in a
26 position where out of a total debt of \$18,599,000,000,
27 only \$8,362,000,000 or 45 per cent is for a fixed period
28 of over 3 years; \$6,158,000,000 or 33 per cent matures
29 in under 3 years and a further \$4,079,000,000 or 22 per
30 cent consists of Canada Savings Bonds which represent a



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1 call on the Government at any time.

2 Marketing of New Issues and Investor Attitudes

3 25. In the last five years large Federal
4 Government deficits have necessitated substantial annual
5 increases in the debt. The marketing of the issues to
6 cover the deficits was made possible to a large extent
7 through the development of the money market. The one
8 attribute which Federal securities should have which is
9 not possessed in the same measure by any other security is
10 their market liquidity. With the concentration by the
11 Federal Government on the mass public market for new
12 funds through the medium of Canada Savings Bonds, this
13 liquidity, or ease of marketability, for fixed term
14 securities has declined in recent years for all but the
15 shorter maturities. This has meant that those financial
16 institutions such as chartered banks, trust companies for
17 their guaranteed investment account and corporations
18 have tended to confine their investments to Government
19 bonds of shorter maturity. In situations where an
20 investor has chosen to buy longer term bonds the tendency
21 has been towards the purchase of provincial, municipal or
22 corporation bonds where a higher yield has been available
23 with ample security and in many cases as satisfactory
24 a degree of marketability due to the operation of sinking
25 funds in the case of provincial and corporate securities.

26 Canada Savings Loans

27 26. Since their introduction in 1946, Canada
28 Savings Bonds have become a significant element both in
29 the debt structure and in the annual public borrowing
30 operations of the Federal Government. Despite sizable

Marketing of New Issues and Investor Attitudes

increase in the debt. The marketing of the issues to cover the deficits was made possible to a large extent through the development of the money market. The one attribute which Federal securities should have which is not possessed in the same measure by any other security is their market liquidity. With the concentration by the Federal Government on the mass public market for new bonds through the medium of Canada Savings Bonds, this liquidity, or ease of marketability, for fixed term securities has declined in recent years for all but the shorter maturities. This has meant that those financial institutions such as chartered banks, trust companies for investment purposes, and other institutions have tended to confine their investments to Government bonds of shorter maturity. In situations where an investor has chosen to buy longer term bonds the tendency has been towards the purchase of provincial, municipal or corporation bonds where a higher yield has been available with ample security and in many cases as satisfactory as Government bonds.

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1 redemptions for cash over the years, the outstanding
2 amount of Savings Bonds has increased year by year since
3 1951 to nearly \$4.1 billion, and is now equal to just
4 under one-quarter of the public debt. To the end of
5 December, applications for the 1961 Series, first offered
6 in October, numbered in excess of 1 1/4 million for over
7 \$932 million of Bonds.

8 27. Savings Bonds are designed for individual
9 investors of modest means but have been bought, within
10 the limitations established for each issue, by larger
11 investors. Being the equivalent of cash, they are the
12 most suitable and have become the most acceptable form
13 of risk-free investment for persons who are unable or
14 unwilling to assume the risks of the price declines which
15 can occur in market type securities. For these reasons,
16 it seems certain that the kind of personal savings
17 mobilized for Government use by the issue of Savings
18 Bonds is, to some extent, a body of funds which would not
19 be invested in other forms of securities if Savings Bonds
20 were not available each year for public purchase.

21 28. While the prime reason for the annual sale
22 of Savings Bonds is to provide part of the cash required
23 to finance Government expenditures, they also serve other
24 important purposes. For example, they encourage the
25 ownership of liquid assets by a large number of families
26 which might not otherwise be inclined to save. Then, by
27 increasing greatly the number of persons who have some
28 direct ownership of securities, the Savings Bond programme
29 over the years has undoubtedly widened public interest
30 in securities.



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...



29. Benefits and advantages of Savings Bonds to the individual investor and to the Canadian economy are costly to the issuer. From available evidence, it is certain they are costly to sell and to service because cash redemptions well before final maturity date constitute a high proportion of original sales. (See Exhibit 4). This means a large part of the funds realized from the sale of each Series is available to Government use for only a relatively short period. Then, because they confer the right of cash redemption, Savings Bonds are, in effect, demand obligations which currently aggregate the sizable magnitude of over \$4 billion. Through control of the money supply, the Federal Government can always pay its debts. But, increasing the money supply to finance debt retirement is not always a sound course of action. For this reason, there could be times when Government borrowing operations to raise funds for Savings Bond redemptions would impose undesirable burdens on the capital market.

30. From this brief outline, it is evident that the economic dangers and financial costs inherent to Savings Bonds impose a limitation on their use as an instrument of debt management policy. Their advantages can be purchased at too high a price. Moreover, their use by borrowers other than the Federal Government involves even greater risks.

31. The great difficulty lies in fiscal policy. Had fiscal policy not led to large deficits in the last few years, it is possible that Savings Loans, as a major money raising vehicle, would not have been used to the

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Had fiscal policy not led to large deficits in the last
few years, it is probable that Savings Bonds, as a means
of raising additional funds, would have been used to the



1 same extent. The solution to the problem lies in smaller
2 deficits on the part of the Federal Government and less
3 reliance on Savings Loans with a greater emphasis on
4 fixed term securities as a means of raising governmental
5 requirements.

6 Recommendation

7 32. We recommend that Canada Savings Loan issues
8 in the future be offered as a pure savings instrument and
9 that the maximum amount available to any one buyer be
10 examined. Originally, Canada Savings Loan issues were
11 made with the idea of educating the small buyer to the
12 theories of thrift, but recently, there has been a
13 tendency to use this method of financing as a major
14 money raising vehicle. The general consensus of opinion
15 of the members of the Investment Dealers' Association is
16 that the maximum amount to any one buyer should not
17 exceed \$5,000 and that the selling emphasis should be in
18 the area of the payroll savings for the small investor.
19 If this approach was taken it would, of course, be
20 necessary, if the demand for new money persists, to raise
21 the greater percentage of the Government's requirements
22 through the medium of issues with a fixed maturity.

23 Federal and Provincial Financing in the Last Ten Years
24 Under Review

25 33. As we entered the 1950's, it was obvious
26 that the investor climate had shifted for reasons outlined
27 in the previous paragraphs and it was therefore no longer
28 possible for the Government to continue to borrow the
29 appropriate portion of its requirements in the long-term
30 sector. It was in this period that the Conversion Loan

Federal and Provincial Financing in the Last Ten Years

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1 of 1958 was conceived as a refunding operation to
2 lengthen the overall maturity of the debt. The provinces,
3 with credit only second to the Government of Canada,
4 could always offer their issues to give a higher yield
5 and the public was demanding a portion of its investment
6 in shares to offset the inflationary tendencies of the
7 economy.

8 34. It was therefore necessary for the
9 Government to tap other sources for their new money
10 requirements. These sources were demanding shorter-term
11 securities with a high degree of liquidity. In line
12 with this demand the Government encouraged the
13 development of the money market at the same time that
14 investor psychology was changing. This enabled the
15 Government to raise its necessary requirements in the
16 short-term area and left the long-term market, except
17 for C.N.R. financing, free for the provinces, and other
18 long-term borrowers. Most provincial borrowing is for
19 long-term projects and long-term debt should be issued
20 against these projects. In some instances, the
21 provinces have used the short-term market for fixed term
22 securities and savings loans and other routes. This
23 method of provincial financing, particularly in the case
24 of provincial savings loans should be limited, as the
25 provinces are not in control of currency and credit.

26 35. It appears to us that it is not vital to
27 have the average term of the Federal debt extended to
28 its absolutely attainable length. However, having in
29 mind that Federal borrowing is not only to finance
30 deficits and refund maturing obligations, but to provide



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method of provincial financing, particularly in the case
of provincial savings loans should be limited, as the
provinces are not in control of currency and credit.
35. It appears to us that it is not vital to
have the average term of the Federal debt extended to
its absolutely attainable length. However, having in
mind that Federal borrowing is not only to finance



1 funds for government agencies who normally require long-
2 term debt, such as the Canadian National Railway, St.
3 Lawrence Seaway, housing, etc., it is only sound
4 practice that our Federal debt should be for a somewhat
5 longer period than its counterpart in the United States
6 where Government agencies also borrow for their own
7 account. In the United States the average term of
8 the marketable debt was 4 years and 7 months as of
9 December 31st, 1961 and the comparable figure for Canada
10 was 8 years and 4 months.

11 36. There will be periods in the future as in
12 the past when depressed conditions in Canada indicate
13 that the money supply can be increased without inflationary
14 implications. This is a time when a greater proportion
15 than otherwise of the investment dollar flows into debt
16 securities. It is in such times that long-term debt
17 can be issued or major conversion opportunities arise
18 for a lengthening of the average term of the Federal
19 debt.

20 RECOMMENDATIONS

21 37.

- 22 1. In times of high business activity,
23 government should budget for surpluses
24 which should be used to retire debt
25 and not for the development of new
26 government spending programmes.
27 Sinking funds on long-term Federal
28 issues, such as exists on provincial
29 debt, would materially assist
30 orderly marketing.



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CONCLUSIONS

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which should be used to retire debt

and not for the development of new

Government spending programs.

Sinking funds on long-term Federal

issues, such as exists on provincial

debt, would materially assist

ordinarily operations



38.

2. Every effort should be made to reduce the Government's reliance on Savings Loan issues as a major money raising vehicle.

39.

3. Because of the nature of provincial requirements, provinces should only resort to short-term Fixed Maturity debt instruments when long-term money is not available.

40.

4. Since the provinces are not in control of currency and credit the use of Savings Loan type of issues should be sharply curtailed.

41. For comparative purposes and in order that a proper assessment of our own methods of financing of the Federal and provincial governments in Canada may be made, it seems appropriate to review the methods employed in the United Kingdom and the United States and draw some conclusions.

Comparison Between Canada and the United Kingdom

42. During the period under review, 1946 to 1961, the market in the United Kingdom for British Government and local authority issues (the latter being the equivalent of our provincial issues) has exerted very little influence on the level of the Canadian high-grade market. In our opinion, therefore, it is unnecessary to make an exhaustive comparison of the two markets,

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except to comment on the different methods employed in the two markets to raise capital for similar types of issues.

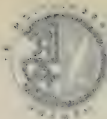
43. In Britain the Bank of England controls the terms and time of issue in the categories under review. There are three main categories used in Britain as follows:

1. Treasury Bills

44. As in Canada, Treasury Bills in Britain come up for tender once a week. Unlike Canada, the British banks do not tender for Bills for their own account, but meet their requirements by purchasing Bills from the discount market, which is comprised of a group of discount houses, nominated by the Bank of England, which are members of the London Discount Market Association, and each week these members put in one composite bid for the entire tender. The British banks and others then purchase their requirements from the discount houses at the then market level.

2. British Government

45. British Government issues are made through the Bank of England which pays a commission to banks and dealers for orders received and accepted. If the issue is not entirely subscribed for in this manner, the issue is announced as having been fully subscribed, the balance being underwritten by the Issue Department of the Bank of England and gradually sold into the market at the going rate by the Government dealer, and the price at which the security is eventually sold is therefore, in effect, the issue price.



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1 3. Local Authorities

2 46. Local authorities, which are in effect the
3 equivalent of our provincial issues, usually employ a
4 dealer to advise them on the terms and conditions of the
5 issue for a fee, usually $1/4$ of 1 per cent. In the
6 first instance an issue is fully underwritten by a group
7 consisting of all types of financial institutions. The
8 underwriting group receives a fee of from $3/4$ per cent
9 to 1 per cent, depending on whether the operation is a
10 conversion offer or to raise new money. In addition to
11 the above charges a commission (allowance) of $1/4$ of 1
12 per cent is paid to banks and dealers on allotments made
13 in respect of their applications. Thus the total costs
14 in this respect are between $1\ 1/4$ per cent and $1\ 1/2$ per
15 cent. The issues are made by public subscription with
16 advertisement in the press inviting applications. If
17 the issue is fully or over-subscribed by such public
18 subscriptions, the underwriting institutions mentioned
19 receive no allotment in respect of their underwriting.
20 Thus if they wish to subscribe to the issue they have to
21 make application along with the rest of the investing
22 public. If the issue is not fully subscribed the
23 underwriters receive their proportion of the unsubscribed
24 amount which is either retained as a permanent investment
25 or sold in the market at the going quotation.

26 RECOMMENDATIONS

27 47.

28 1. The method employed in Canada for Treasury
29 Bill financing seems more suitable than the method employed
30 in the United Kingdom for this market. The "one bid"

RECOMMENDATIONS

46. Local authorities, which are in effect the equivalent of our provincial issues, usually employ a dealer to advise them on the terms and conditions of the issue for a fee, usually $1\frac{1}{4}$ of 1 per cent. In the first instance an issue is fully underwritten by a group consisting of all types of financial institutions. The underwriting group receives a fee of from $3\frac{1}{4}$ per cent to 1 per cent, depending on whether the operation is a conversion offer or to raise new money. In addition to the above charges a commission (allowance) of $1\frac{1}{4}$ of 1 per cent is paid to banks and dealers on allotments made in respect of their applications. Thus the total costs in this respect are between $1\frac{1}{4}$ per cent and $1\frac{1}{2}$ per cent. The issues are made by public subscription with advertisement in the press inviting applications. If the issue is fully or over-subscribed by such public applications, the underwriting institutions mentioned receive no allotment in respect of their underwriting. Thus if they wish to subscribe to the issue they have to make application along with the rest of the investing public. If the issue is not fully subscribed the underwriters receive their proportion of the unsubscribed amount which is either retained as a permanent investment or sold in the market at the going quotation.

RECOMMENDATIONS

47. The method employed in Canada for Treasury



1 method employed in Britain is suited to the special
2 conditions of that market and is not strictly comparable
3 with the method of operation in Canada.

4 48.

5 2. Direct British Government financing is
6 carried on in much the same manner as in Canada except
7 that in Canada it has been the practice of the Bank of
8 Canada, acting as agents for the Government, to give
9 dealers a firm amount of bonds on announcement of the
10 new issue in order that confirmation can be given to the
11 dealers' customers. We feel that the system employed in
12 Canada is more appropriate for our market in that it
13 allows immediate confirmation to the customer and gives
14 dealers the ability to accurately appraise the demand
15 when they subscribe for additional bonds.

16 49.

17 3. The financing of local authorities is
18 similar to the way our provinces are financed in Canada
19 insofar as they are done through a dealer manager, but
20 at this stage the similarity stops. All the manager
21 does is set the issue up for a fee and then orders may
22 flow in direct to the local authority and allotments are
23 made.

24 50.

25 4. In the case of Canadian provincial issues,
26 the most accepted and, in our opinion, the best method
27 is to appoint a manager, who forms a strong group of
28 underwriters. After consultation with the borrower and
29 the senior members of the underwriting group, a bid for
30 all or part of the issue is made to the province

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4. In the case of Canadian provincial issues, the most accepted and, in our opinion, the best method is to appoint a manager, who forms a strong group of underwriters. After consultation with the borrower and the senior members of the underwriting group, a bid for all or part of the issue is made to the province



1 concerned. It is then the responsibility of the dealer
2 group to merchandise the securities in which it has a
3 definite liability. The fact that the group has a
4 liability makes it essential that it distributes the
5 securities as quickly as possible and also develops for
6 the province concerned the most widespread and steady
7 market for its issue.

8 Comparison Between Canada and the United States

9 51. Because of the importance which the United
10 States Government bond market exerts on the Canadian
11 Government bond market, a more thorough review seems to
12 be in order. Basically, the interest rates in the United
13 States and in Canada bear a definite relationship and
14 since we in Canada operate in the dollar area, there is a
15 substantial flow of capital between the two countries.
16 This flow has the effect of arbitrage and tends to keep
17 what is regarded as a proper yield spread between the two
18 markets, taking into account the yield obtainable in the
19 comparable credits of the two markets and the level of
20 our dollar in relation to the United States dollar. The
21 essential difference between Canada and the United States
22 in the distribution of direct Federal government
23 securities lies in the lack of any compensation in the
24 United States to dealers and dealer banks through whom
25 the issues eventually reach the investor.

26 52. In a country such as the United States
27 which has reached the stage in its development where it is
28 creating savings at a greater rate than they can be
29 employed, this system can perhaps be justified. It does,
30 however, mean that Government issues handled in this way



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Relationship Between Canada and the United States

51. Because of the importance which the United States Government bond market exports on the Canadian Government bond market, a more thorough review seems to be in order. Basically, the interest rates in the United States and in Canada bear a definite relationship and since we in Canada operate in the dollar area, there is a substantial flow of capital between the two countries. This flow has the effect of arbitrage and tends to keep what is regarded as a proper yield spread between the two markets, taking into account the yield obtainable in the comparable credits of the two markets and the level of our dollar in relation to the United States dollar. The essential difference between Canada and the United States in the distribution of direct Federal Government securities lies in the lack of any compensation in the United States to dealers and dealer banks through whom the issues eventually reach the investor.

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1 do not find their way into the broad public market.
2 There is therefore no public market such as we have in
3 Canada for Government securities. So United States
4 Government debt securities tend to be held in the main by
5 Government accounts, banks, insurance companies, trust
6 companies, pension funds and other semi-institutional
7 pools of investment capital. This is accounted for by
8 the tax exempt United States State bonds being available
9 to private investors in the United States and not in
10 Canada.

11 Government Treasury Bill Market

12 53. The Government Treasury Bill market is
13 handled much the same as in Canada. These Bills are
14 sold at auction once a week. A group of seventeen
15 accredited dealers and banks, which have been recognized
16 as purchasers by the Open Market Committee, bid on the
17 Bills, and market them in a similar way to that which
18 is employed in Canada.

19 54. In the United States the equivalent of the
20 provincial issues are the State issues. The method of
21 marketing is similar in some ways to the Canadian method
22 in that new issues are either sold by public tender to
23 a group of dealers of whom one is the manager, or the
24 manager of a group negotiates the price and terms on
25 behalf of his group. The marketing then takes place in
26 a similar way to that which is employed in Canada.

27 55. All State issues in the United States are
28 exempt from all Federal income taxes and the obligations
29 of any State are exempt from any State income taxes
30 levied by that State. As a result of the tax exempt



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Government Securities Bill

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55. All State issues in the United States are exempt from all Federal income taxes and the obligations of any State are exempt from any State income taxes



1 feature on State issues, the yield is relatively low and
2 the demand comes, not from the broad general public, but
3 from wealthy individuals and companies where the tax
4 feature has an important bearing. This precludes any
5 broad public distribution in the sense that we understand
6 it in Canada.

7 (Paragraph 56 deleted intentionally).

8 57.

9 1. No recommendations seem necessary as far
10 as the method of handling Treasury Bills in our market is
11 concerned. It is pointed out, however, that in the United
12 States, the seventeen accredited dealers and banks are
13 the only bidders, whereas in Canada any dealer can make
14 a bid at the auction. Although in practice only the
15 dealers nominated to the money market make a bid.

16 58.

17 2. The method used by the United States
18 Federal Government to raise money would not, in our
19 opinion, do the job in Canada. The fact that the United
20 States government pay no concession for distribution means
21 that their distribution is limited as pointed out in
22 previous paragraphs. The one thing which is required
23 in Canada is widespread public distribution and this can
24 only be secured by paying the dealers a compensation for
25 distribution.

26 59.

27 3. In view of the fact that United States
28 State bonds are exempt from Federal Taxation and also
29 exempt from any State income taxes levied by that State,
30 it is difficult to derive any definite conclusions



feature on State issues, the yield is relatively low and the interest comes, not from the broad general public, but from wealthy individuals and companies where the tax feature has an important bearing. This provides any distribution in the same way as it is in Canada.

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1 between the two markets.

2 Marketing of New Issues

3 60. We have discussed marketing procedures in
4 Great Britain and the United States. The following
5 paragraphs will be devoted to the marketing of new
6 Government of Canada and provincial issues in Canada.

7 Government of Canada Issues

8 61. The timing and terms of Government of
9 Canada issues are determined by the Finance Department
10 on advice from its agent, the Bank of Canada. The
11 amount required in any one year is determined by the
12 amount of maturing obligations in that year, plus the
13 new money requirements, if any. During the first ten
14 years under review, the Federal Government enjoyed
15 surpluses, with the exception of 1946 and 1955, and
16 their outstanding unmatured debt decreased from
17 \$17,313,000,000 in 1946 to \$15,334,000,000 in 1951 and
18 \$15,234,000,000 in 1956. The marketing, therefore, of
19 new issues was almost entirely confined to refunding and
20 did not present a problem of any great magnitude.
21 However, in the last five years, with one exception, the
22 Federal Government has experienced large deficits, with
23 the result that the problem of new public issues has been
24 considerably expanded as witnessed by the increases in
25 the Federal debt to \$18,599,000,000 as at December 31st,
26 1961.

27 62. Various techniques have been evolved
28 through experience. Recently new issues have been
29 confined to the short-term area which has allowed other
30 borrowers, such as the provinces, to enjoy as much



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the Federal debt to \$18,599,000,000 as at December 31st,

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62. Various techniques have been evolved

through experience. Recently new issues have been
confined to the short-term ones which has allowed other

borrowers, such as the provinces, to enjoy as much



1 freedom as possible in the long-term market. All
2 Government issues have been marketed through normal
3 dealer channels and with some exceptions firm
4 participations have been given to dealers for distribution
5 to their customers.

6 63. There has been some criticism that the list
7 of primary distributors are, in fact, not normally
8 engaged in the distribution of Government securities and
9 it is recommended that the list of primary distributors
10 be thoroughly overhauled in order that the best possible
11 public distribution be secured for the Government under
12 present conditions. Another point which deserves study
13 is the recent trend towards new issues by the Government,
14 being taken up entirely by the Bank of Canada and then
15 marketed at a later date. Between the time these issues
16 are announced and the time they are available in the
17 market, the dealer must make an educated guess on what
18 the price will be and hope to provide fair value to the
19 investor. This does not induce proper widespread
20 distribution and does foster a certain amount of
21 speculation which is undesirable, particularly in the
22 securities of the Government of Canada.

23 64. The price of the issue, which is entirely
24 taken up by the Bank of Canada and marketed in the manner
25 outlined above, is publicly announced. The price at
26 which the issue is traded one week later inevitably is
27 either above or below the announced issue price with
28 all the market repercussions which this sort of an
29 operation creates. In addition, the issue price may
30 be too high and subsequent demand therefore so limited

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of primary distributors are, in fact, not actually engaged in the distribution of Government securities and it is recommended that the list of primary distributors be thoroughly overhauled in order that the best possible public distribution be secured for the Government under present conditions. Another point which deserves study is the recent trend towards new issues by the Government, being taken up entirely by the Bank of Canada and then marketed at a later date. Between the time these issues are announced and the time they are available in the market, the dealer must make an educated guess on what the price will be and hope to provide fair value to the investor. This does not induce proper widespread distribution and does foster a certain amount of speculation which is undesirable, particularly in the securities of the Government of Canada.

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1 that a very small percentage is held by the public with
2 a consequent thin after-market.

3 RECOMMENDATIONS ON GOVERNMENT FINANCING

4 65. In order that the experience and technical
5 marketing skills and knowledge of the investment industry,
6 which is in close and daily touch with the ultimate
7 buyer of Government of Canada securities, be effectively
8 centralized and made available to the debt managers, it
9 is recommended that a standing committee on the marketing
10 of Government of Canada Bonds be established by
11 government decree. This committee would act in an
12 advisory capacity to the Bank of Canada and the
13 Department of Finance in connection with the marketing
14 of Government of Canada issues and problems arising
15 therefrom or related thereto. It should be comprised
16 of men of experience and independent judgment in the
17 field of Government finance drawn from the investment
18 industry and, if deemed necessary, from other segments
19 of the financial community. The Committee should be
20 workable in size to facilitate decision-making and ease
21 of consultation in Ottawa when requested by the Bank of
22 Canada and/or the Department of Finance. Its composition
23 should recognize the geographical location of the various
24 financial centres of Canada with appropriate weight being
25 given to their size and importance.

26 RECOMMENDATIONS ON C.N.R. FINANCING

27 66. As a result of the success of provincial
28 financing through large national syndicates it is
29 recommended that future Canadian National Railway or
30 other Government agencies which require long-term



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- 11 -

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RECOMMENDATIONS ON C.M.R. FINANCING

66. As a result of the success of provincial

financing through large national syndicates it is recommended that future Canadian National Railway or other Government securities which require long-term



1 should be handled in a similar way to that of the
2 financing of the larger provinces. That is, a large
3 national syndicate should be formed headed by a dealer
4 or group of dealers to be chosen by the Department of
5 Finance in consultation with the C.N.R. and the Bank of
6 Canada. In fact, there was in existence until such
7 financing came under the direction of the Bank of Canada.
8 The manager, or managers, would then form a banking group
9 composed of the dealers in Canada, who usually underwrite
10 and take a liability and who would be available for
11 prior consultation on timing, size, maturities and prices
12 of new issues to be brought to the market. In addition
13 to this, there should be a selling group of all other
14 distributors of Government securities in Canada. There
15 will inevitably be some dealers who are designed as
16 selling group members, who will feel they should be
17 members of the banking group. Their proven distributing
18 power would be the deciding factor as to whether they
19 are members of the banking group or the selling group,
20 and this should be decided in consultation with the
21 C.N.R., the Finance Department, the Bank of Canada and
22 the management group.

23 Provincial Financing

24 67. As we entered the 1950s, it was obvious
25 that the investor climate had shifted for reasons
26 outlined in the opening paragraphs of this Brief and it
27 was at this time that the requirements of the provinces
28 were becoming very large as a result of huge expenditures
29 which had to be made for hospitals, roads, schools,
30 public utilities, etc.



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were becoming very large as a result of huge expenditures
which had to be made for hospitals, roads, schools,



1 68. It was in this period that the Bank of
2 Canada, with the assistance of the chartered banks and
3 money market dealers, formed the money market, which
4 developed a far broader and deeper market for Federal
5 Government Treasury Bills and Federal Government market
6 issues maturing in less than three years and this enabled
7 the Federal Government to raise the major portion of its
8 requirements in this area leaving the longer term markets
9 available to the provinces, which due to the nature of
10 their requirements should, under most circumstances,
11 borrow their requirements in the long-term market.

12 69. Since there are not enough large pools of
13 money in Canada to finance the requirements of the
14 provincial governments, it has become increasingly
15 evident that broad public distribution is the only way
16 in which the provinces could raise their requirements.
17 It is apparent that these large requirements can only be
18 raised through the medium of continuing strong national
19 syndicates, with the exception of provinces whose
20 requirements are not large.

21 70. The issues are usually negotiated by the
22 syndicate manager, who has the benefit of advice from
23 what is known as a steering committee. This committee
24 is made up of qualified persons from members of the
25 syndicate whose judgment have been time proven. Once
26 the price and terms have been settled the syndicate,
27 which is handling the issue, takes a liability. This
28 liability is the driving force behind the dealer
29 fraternity to distribute the securities to the public
30 and is one of the reasons why there is such a broad,



68. It was in this period that the Bank of Canada, with the assistance of the chartered banks and other financial institutions, developed a far broader and deeper market for Federal Government Treasury Bills and Federal Government market issues maturing in less than three years and this enabled the Federal Government to raise the major portion of its requirements in this area leaving the longer term markets available to the provinces, which due to the nature of their requirements could not borrow their requirements in the long-term market.

69. Since there are not enough large pools of money in Canada to finance the requirements of the provincial governments, it has been necessary to develop that broad public distribution as the only way in which the provinces could raise their requirements. It is apparent that these large requirements can only be raised through the medium of continuing strong national syndicates, with the exception of provinces whose requirements are not large.

70. The issues are usually negotiated by the syndicate manager, who has the benefit of advice from what is known as a steering committee. This committee is made up of qualified persons from members of the syndicate whose judgment have been time proven. Once the price and terms have been settled the syndicate, which is handling the issue, takes a liability. This liability is the driving force behind the dealer's responsibility to distribute the securities to the public and is one of the reasons why there is such a broad



1 healthy interest in provincial issues. The syndicate
2 also has a further responsibility of continuing to
3 foster the market for provincial securities between new
4 issues and keep the provinces informed of market
5 conditions. We cannot stress too strongly the fact that
6 provincial borrowing is for long-term projects and long-
7 term debt should be issued against these projects. In
8 some instances, the provinces have used the short-term
9 market for dated securities and savings loans and other
10 routes. This method of provincial financing, particularly
11 in the case of provincial savings loans, should be
12 limited as the provinces are not in control of currency
13 and credit.

14 Method of Distributing Provincial Securities to the
15 Public

16 71. Whether the distribution of provincial
17 securities to the public is made through a single dealer
18 or a syndicate composed of a number of dealers, the
19 process is the same. The issue is either purchased by
20 public tender or the purchase is at a negotiated price.
21 Once this has taken place the issue is set up to offer
22 to the public. The retail price is set, concessions
23 to sub-agents and dealers announced to the trade, and a
24 decision is reached as to whether there will be a selling
25 group or not. The decision to have a selling group is
26 governed by the size of the issue. On relatively small
27 issues, widespread distribution is not required and,
28 therefore, there would not normally be a selling group,
29 but on larger issues, there usually is a selling group
30 and this group is usually composed of members of the

healthy interest in provincial issues. The syndicate also has a further responsibility of continuing to foster the market for provincial securities between new issues and keep the provinces informed of market conditions. We cannot stress too strongly the fact that provincial borrowing is for long-term projects and long-term debt should be issued against these projects. In some instances, the provinces have used the short-term market for dated securities and savings loans and other routes. This method of provincial financing, particularly in the case of provincial savings loans, should be limited as the provinces are not in control of currency and credit.

Method of Distributing Provincial Securities to the Public

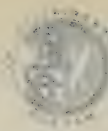
VI. Whether the distribution of provincial securities to the public is made through a single dealer or a syndicate composed of a number of dealers, the process is the same. The issue is either purchased by public tender or the purchase is at a negotiated price. Once this has taken place the issue is set up to offer to the public. The retail price is set, concessions to sub-agents and dealers announced to the trade, and a decision is reached as to whether there will be a selling group or not. The decision to have a selling group is governed by the size of the issue. On relatively small issues, widespread distribution is not required and, therefore, there would not normally be a selling group, but on larger issues, there usually is a selling group and this group is usually composed of members of the



1 I.D.A. who are not the original buyers of the issue or
2 who are not in the syndicate who purchase the issue.

3 72. The terms are set and usually 50 per cent
4 to 60 per cent of the issue is confirmed to the under-
5 writing group for sale to their clients. The remainder
6 is reserved for the exempt institutions and selling
7 group. Exempt institutions are made up of all the large
8 insurance companies, trust companies and banks. The
9 amount of bonds purchased by the exempt institutions
10 varies very widely depending on the amount of money they
11 have available for investment at the time. The amount
12 of bonds confirmed to the selling group varies to some
13 extent depending on the size of the issue, with the
14 selling group usually receiving a larger percentage of
15 the amount on large issues. In small issues adequate
16 allotments to the selling group present a problem for
17 the 189 members of the I.D.A.

18 73. If exempt institutions and the selling
19 group do not subscribe for the amount set aside for
20 them it is obviously the liability of the originating
21 group to absorb this amount into their own book and do
22 the distribution themselves. If the selling group
23 dealers subscribe for more than is normally available
24 to them the originating syndicate tries to make a further
25 amount available out of their own firm bonds or perhaps
26 take a short position not only for after-market
27 operations but in order that selling group members get
28 as fair treatment as possible under the market conditions
29 then existing.
30



...the original paper of the issue...

who are not in the syndicate who purchase the issue.

72. The terms are set and usually 50 per cent

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RECOMMENDATIONS

74.

1. Due to the nature of provincial requirements provinces should only resort to short-term fixed maturity debt instruments when long-term money is not available.

75.

2. Since the provinces are not in control of currency and credit, the use of savings loan types of issues should be sharply curtailed.

76.

3. We recommend that provincial financing, except for small issues should be handled by large national syndicates headed by the managing firm, which in turn should be backed up by a steering committee composed of qualified persons from members of the syndicate. It is in this way that a continuous broad, healthy market will be maintained for provincial securities in Canada.

REFERENCES

SUMMARY OF RECOMMENDATIONS

The Association recommends:

Pr. 13
Pages A.170
to A.171

(a) that Government of Canada issues with maturities in excess of three years should have an annual sinking fund of 1 per cent of their principal amount;

Pr. 14
Page A.171

(b) that the Commission enquire as to whether debt management and control of currency have conflicting interests and whether these should be separated.



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- (b) that the Commission enquire as to whether debt management and control of currency have conflicting interests and whether these should be separated.
- Tr. 14
Page A.171



(c) that the Commission should enquire
into whether Bank of Canada or some
other agency should operate the purchase
fund and government accounts.

(d) that consideration be given to
establishing two separate bank rates as
follows:

(i) a rediscount rate for chartered
banks and money market dealers
established on the basis as the
present so-called "floating rate",
and

(ii) a fixed Bank Rate to signal
important changes in monetary
policy and consequently the prime
lending rate of Chartered Banks;

(e) that the Government reiterate its
belief in the generally accepted basic
principles of responsible debt management;

(f) that serious consideration be given
to changing the 1962 fall Savings Loan
Campaign by combining a smaller Canada
Savings Loan issue with a fixed term
issue;

(g) (i) that the Government should budget
for surpluses in periods of high business
activity for the purpose of debt
retirement;

(ii) that the Government rely less on
Canada Savings Bonds as a major vehicle

(c) that the Government should subject

Pr. 16

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Pr. 16
A.172
Pr. 31
A.172 and A.173

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Pr. 26
Pages A.175
and A.176

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for supplies in periods of high business

activity for the purpose of debt

retirement;

(ii) that the Government rely less on

Pr. 33
Page A.177
Pr. 40
Page A.181



1 for raising money;

2 (iii) that Provincial Governments
3 sharply curtail the use of Savings Loans
4 type of issues as a money-raising vehicle
5 and only use short-term fixed debt
6 instruments for such purposes when long-
7 term money is not available;

8 (h) that the present methods employed in
9 Canada for Treasury Bill financing, the
10 direct placement of Government of Canada
11 issues and the underwriting of Provincial
12 issues be continued in preference to the
13 methods used in the United Kingdom for
14 comparable issues in that market;

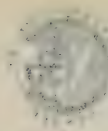
15 (i) that the present methods employed in
16 Canada for Treasury Bill financing, the
17 direct placement of Government of
18 Canada issues and the underwriting of
19 Provincial issues, while similar in many
20 respects to United States practises, be
21 continued in preference to the methods
22 used in the United States for comparable
23 issues in that market;

24 (j) that a standing committee on the
25 marketing of Government of Canada Bonds,
26 to comprise men from the financial
27 community having experience and independent
28 judgment in the marketing of Government of
29 Canada Bonds, be established by Government
30 decree to act in an advisory capacity

Pr. 42,
Page A.181
to
Pr. 50
Page A.184

Pr. 51,
Page A.185
to
Pr. 59
Page A.187

Pr. 61,
Page A.188
to
Pr. 65,
Page A.190



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sharply curtail the use of Savings Bonds
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Canada for Treasury Bill financing, the

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methods used in the United Kingdom for

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direct placement of Government of

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respects to United States practices, be
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marketing of Government of Canada Bonds,

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Pr. 51,
Page A.185
to
Pr. 52
Page A.184

Pr. 51,
Page A.185
to
Pr. 52
Page A.187

Pr. 61,
Page A.188
to
Pr. 62,
Page A.190



1 to the Bank of Canada and the Department
2 of Finance in connection with the
3 marketing of Government of Canada
4 issues;

5 (k) that future financing of the Canadian
6 National Railways, and other Government
7 agencies requiring long-term financing,
8 be arranged through large national
9 syndicates of investment dealers managed
10 by one or more dealers selected by the
11 Department of Finance in consultation
12 with the Canadian National Railways and
13 the Bank of Canada;

14 (1) that Provincial financing, except
15 small issues, should continue to be

16 Pr. 67, arranged through large national
17 Page A.191 syndicates of investment dealers
18 to
19 Pr. 76, managed by one or more dealers backed
20 Page A.195 up by a steering committee composed
21 of qualified persons selected from
22 members of the syndicate.

23 ---O---



A. 191

Page 191

to the Bank of Canada and the Department
of Finance in connection with the
marketing of Government of Canada

through

(k) that future financing of the Canadian
National Railways, and other Government
operated railways, including

be arranged through large national
syndicates of investment dealers managed
by one or more dealers selected by the
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with the Canadian National Railways and
the Bank of Canada;

(l) that future financing, and

small issues, should continue to be

arranged through large national

syndicates of investment dealers

managed by one or more dealers selected

up by a steering committee composed

of qualified persons selected from

members of the syndicate.

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A. 190 to
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A. 191

EXHIBIT 1

<u>Issue</u>	<u>Sinking Fund</u>
Province of Alberta Municipal Financing Corporation	2% of the principal amount annually.
Province of Manitoba	1% to 3% of the principal amount annually.
Manitoba Hydro-Electric Board	1% of the principal amount annually plus 4% on balance in the Sinking Fund Account.
Province of New Brunswick	2% to 3% of the principal amount annually.
Province of Newfoundland	1 3/4% to 3% of the principal amount annually.
Province of Nova Scotia	3% of the principal amount annually.
Province of Ontario	Appropriations made annually to a general sinking fund. Several issues have specified sinking fund arrangements.
Hydro-Electric Power Commission of Ontario	Annuity method, using a 4% interest rate, applied to value of operating properties which are written off over 40 years.
Province of Prince Edward Island	3% of the principal amount annually.
Province of Saskatchewan	3% of the principal amount annually.
Province of Quebec	1% of the principal amount annually.
Quebec Hydro-Electric Commission	1% of the principal amount annually with respect to shorter maturities and 2% of the principal amount annually with respect to longer maturities.



EXHIBIT 1

Issue	Sinking Fund
Province of Alberta Municipal Electric Corporation	2% of the principal amount annually.
Province of Manitoba	1% to 2% of the principal amount annually.
Province of Ontario Hydro-Electric Power Commission	1% of the principal amount annually plus 1% on balance in the Sinking Fund Account.
Province of New Brunswick	2% to 3% of the principal amount annually.
Province of Newfoundland	1 3/4% to 2% of the principal amount annually.
Province of Nova Scotia	2% of the principal amount annually.
Province of Ontario	Appropriations made annually to a general sinking fund. Several issues have specified sinking fund percentages.
Province of Ontario Hydro-Electric Power Commission	Annuity method, using a 4% interest rate, applied to value of operating properties which are written off over 40 years.
Province of Prince Edward Island	2% of the principal amount annually.
Province of Saskatchewan	2% of the principal amount annually.
Province of Quebec	1% of the principal amount annually.
Province of Quebec Hydro-Electric Power Commission	1% of the principal amount annually with respect to shorter maturities and 2% of the principal amount annually with respect to longer maturities.

EXHIBIT II
DISTRIBUTION OF GOVERNMENT OF CANADA SECURITIES

As at December 31st

(in millions of par value)

Year	Total Debt	Bank of Canada	Chartered Banks	As % of Total Debt	Govt. of Canada Accounts	As % of Total Debt	General Public Holdings		As % of Total Debt
							Market* Non-Market**	Total	
1946	17,313	1,904	3,317	11.00%	918	5.30%	9,937	11,174	64.54%
1951	15,334	2,222	2,830	14.49	1,009	6.58	8,079	9,273	60.47
1956	15,234	2,426	2,524	15.92	1,518	9.96	6,225	8,766	57.55
1961/	18,599	2,856	3,786	15.35	658	3.54	7,221	11,300	60.75

* This denotes the amount of the Federal Government debt held by the General Public exclusive of Savings Loan Bonds.

** This denotes the amount of Savings Loan Bonds held by the General Public.

/ As at January 2, 1962 from figures supplied by the Bank of Canada.

Source: Bank of Canada "Statistical Summary Supplement 1960"
Government of Canada Direct and Guaranteed Securities
Distribution of Holdings.

February 14, 1962.

1000

1000

DEPARTMENT OF MINISTERS
GOVERNMENT OF CANADA
1000

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(in millions of dollars)

As at December 31st

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Toronto, Ontario

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EXHIBIT III
DISTRIBUTION OF GOVERNMENT OF CANADA SECURITIES

Year	Total Debt	Average Term (excl. Savings & Perpetuals**) Years and Months	Under 3 Years as % of Total Debt	Population	Debt Per Capita***
1946	\$ 17,313	9 - 11	18.55%	12,292,000	\$1,408.48
1951	15,334	7 - 6	24.07	14,009,429	1,095.12
1956	15,234	6 - 7	31.03	16,080,791	947.34
1961	18,599	8 - 4	33.11	18,400,000	1,010.82

* In millions

** Savings Loan Bonds and Perpetuals have been excluded in arriving at the average term due to the fact that Savings Loan Bonds may be cashed at any time at the holder's option and the Perpetuals have no fixed maturity.

*** The debt per capita represents all outstanding debt.

Source: Bank of Canada "Statistical Summary Supplement 1960", Bank of Canada Statements and from figures supplied by the Bank of Canada.

February 14, 1962.



EXHIBIT IV (a) CANADA SAVINGS BONDS

It has been assumed that the amount of each issue outstanding at January 1st represents the total sales of such issue. The January 1st figure represents on the average approximately 90 per cent of total sales.

Total Sales (1946 Series 1 to 1961 Series 16)	\$10,408,715,000
Total Amount outstanding as at January 1, 1962	<u>4,079,000,000</u>
Amount of Redemption and Maturities	\$ 6,329,715,000
Total amount of issues maturing during period (1947-1961)	<u>\$ 1,503,172,000</u>
Resulting amount of Redemption during period (1947-1961)	\$ 4,826,543,000

Redemption as a percentate of Total Sales	46.4%
Maturing issues as a percentate of the Total Sales	14.4%
Total Amount at January 1, 1962 as a percentage of Total Sales	<u>39.2%</u>
	100.0%

February 14, 1962.

EXHIBIT IV (A)

UNITED STATES GOVERNMENT

It has been assumed that the amount of each issue outstanding at January 1st represents the total sales of such issue. The January 1st figure represents on the average approximately 90 per cent of total sales.

Total Sales (1946 Series 1 to 1961 Series 16)	\$10,408,715,000
Total Amount outstanding as at January 1, 1962	\$4,973,000,000
Amount of Redemption and Maturities	\$ 6,320,715,000
Total amount of issues maturing during period 1962-1963	\$ 1,115,715,000
Resulting amount of Redemption	\$ 4,826,543,000

Redemption as a percentage of Total Sales	46.4%
Maturing issues as a percentage of the Total Sales	14.1%
Total Amount at January 1, 1962 as a percentage of Total Sales	39.7%
	100.0%

EXHIBIT IV (B)

EXHIBIT IV (b)

CANADA SAVINGS BONDS

ANNUAL AMOUNTS OUTSTANDING

AS OF JANUARY 1st

(Thousands of Dollars)

Year	Series 1 (1946)	Series 2 (1947)	Series 3 (1948)	Series 4 (1949)	Series 5 (1950)	Series 6 (1951)	Series 7 (1952)	Series 8 (1953)	Series 9 (1954)	Series 10 (1955)	Series 11 (1956)	Series 12 (1957)	Series 13 (1958)	Series 14 (1959)	Series 15 (1960)	Series 16 (1961)	Total	Net Dollar Increase	Total Sales Of Issue *
1947	\$469,251	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$469,251	\$469,251	\$535,285,550
1948	416,965	256,014	-	-	-	-	-	-	-	-	-	-	-	-	-	-	672,977	203,726	287,773,100
1949	378,296	201,795	230,929	-	-	-	-	-	-	-	-	-	-	-	-	-	771,020	86,043	260,491,150
1950	292,237	160,893	176,205	282,856	-	-	-	-	-	-	-	-	-	-	-	-	912,191	141,171	320,200,000
1951	252,296	135,634	137,027	214,182	264,122	-	-	-	-	-	-	-	-	-	-	-	999,261	87,070	285,600,000
1952	206,361	109,771	104,719	153,970	166,551	351,474	-	-	-	-	-	-	-	-	-	-	1,092,606	93,345	394,642,400
1953	175,371	92,901	87,205	124,799	118,738	265,610	331,966	-	-	-	-	-	-	-	-	-	1,198,990	106,184	380,761,100
1954	99,704	52,995	46,642	71,208	66,708	173,342	219,516	840,633	-	-	-	-	-	-	-	-	1,572,738	373,946	850,548,900
1955	72,717	38,641	35,756	52,603	48,928	152,747	173,354	722,874	792,356	-	-	-	-	-	-	-	2,089,976	517,238	800,540,900
1956	58,306	31,142	28,682	42,357	39,049	139,557	154,913	647,549	628,363	649,024	-	-	-	-	-	-	2,419,722	329,746	729,100,000
1957	-	22,937	21,075	31,449	28,752	120,783	137,708	579,720	369,189	404,225	792,441	-	-	-	-	-	2,504,279	88,557	853,810,150
1958	-	-	14,768	22,326	20,399	82,481	97,185	386,510	203,364	208,935	395,534	1,164,766	-	-	-	-	2,596,268	87,989	1,216,711,900
1959	-	-	-	17,227	15,695	62,348	75,035	294,456	147,279	148,945	273,702	1,017,608	835,199	-	-	-	2,887,294	291,026	923,697,450
1960	-	-	-	-	11,277	37,662	41,667	148,566	86,929	85,423	145,868	792,967	444,283	1,398,794	-	-	3,203,436	316,142	1,536,050,600
1961	-	-	-	-	-	30,663	33,042	135,890	68,725	67,135	114,642	720,467	348,825	1,271,407	815,724	-	3,584,480	383,044	960,462,000
1962	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	932,346	4,079,000	492,520

* Figures are for entire loans, either to the closing date within the year or in the subsequent year.

Sources: Bank of Canada Loans of Government of Canada and loans Guaranteed by The Government of Canada 1947 - 1961.
Canada Year Book, 1961.

February 1962.

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STATE OF NEW YORK

OFFICE OF THE COMPTROLLER

REPORT

FOR THE YEAR 1911

Item	1911	1910	1909	1908	1907	1906	1905	1904	1903	1902	1901	1900	1899	1898	1897	1896	1895	1894	1893	1892	1891	1890	1889	1888	1887	1886	1885	1884	1883	1882	1881	1880	1879	1878	1877	1876	1875	1874	1873	1872	1871	1870	1869	1868	1867	1866	1865	1864	1863	1862	1861	1860	1859	1858	1857	1856	1855	1854	1853	1852	1851	1850	1849	1848	1847	1846	1845	1844	1843	1842	1841	1840	1839	1838	1837	1836	1835	1834	1833	1832	1831	1830	1829	1828	1827	1826	1825	1824	1823	1822	1821	1820	1819	1818	1817	1816	1815	1814	1813	1812	1811	1810	1809	1808	1807	1806	1805	1804	1803	1802	1801	1800	1799	1798	1797	1796	1795	1794	1793	1792	1791	1790	1789	1788	1787	1786	1785	1784	1783	1782	1781	1780	1779	1778	1777	1776	1775	1774	1773	1772	1771	1770	1769	1768	1767	1766	1765	1764	1763	1762	1761	1760	1759	1758	1757	1756	1755	1754	1753	1752	1751	1750	1749	1748	1747	1746	1745	1744	1743	1742	1741	1740	1739	1738	1737	1736	1735	1734	1733	1732	1731	1730	1729	1728	1727	1726	1725	1724	1723	1722	1721	1720	1719	1718	1717	1716	1715	1714	1713	1712	1711	1710	1709	1708	1707	1706	1705	1704	1703	1702	1701	1700	1699	1698	1697	1696	1695	1694	1693	1692	1691	1690	1689	1688	1687	1686	1685	1684	1683	1682	1681	1680	1679	1678	1677	1676	1675	1674	1673	1672	1671	1670	1669	1668	1667	1666	1665	1664	1663	1662	1661	1660	1659	1658	1657	1656	1655	1654	1653	1652	1651	1650	1649	1648	1647	1646	1645	1644	1643	1642	1641	1640	1639	1638	1637	1636	1635	1634	1633	1632	1631	1630	1629	1628	1627	1626	1625	1624	1623	1622	1621	1620	1619	1618	1617	1616	1615	1614	1613	1612	1611	1610	1609	1608	1607	1606	1605	1604	1603	1602	1601	1600	1599	1598	1597	1596	1595	1594	1593	1592	1591	1590	1589	1588	1587	1586	1585	1584	1583	1582	1581	1580	1579	1578	1577	1576	1575	1574	1573	1572	1571	1570	1569	1568	1567	1566	1565	1564	1563	1562	1561	1560	1559	1558	1557	1556	1555	1554	1553	1552	1551	1550	1549	1548	1547	1546	1545	1544	1543	1542	1541	1540	1539	1538	1537	1536	1535	1534	1533	1532	1531	1530	1529	1528	1527	1526	1525	1524	1523	1522	1521	1520	1519	1518	1517	1516	1515	1514	1513	1512	1511	1510	1509	1508	1507	1506	1505	1504	1503	1502	1501	1500	1499	1498	1497	1496	1495	1494	1493	1492	1491	1490	1489	1488	1487	1486	1485	1484	1483	1482	1481	1480	1479	1478	1477	1476	1475	1474	1473	1472	1471	1470	1469	1468	1467	1466	1465	1464	1463	1462	1461	1460	1459	1458	1457	1456	1455	1454	1453	1452	1451	1450	1449	1448	1447	1446	1445	1444	1443	1442	1441	1440	1439	1438	1437	1436	1435	1434	1433	1432	1431	1430	1429	1428	1427	1426	1425	1424	1423	1422	1421	1420	1419	1418	1417	1416	1415	1414	1413	1412	1411	1410	1409	1408	1407	1406	1405	1404	1403	1402	1401	1400	1399	1398	1397	1396	1395	1394	1393	1392	1391	1390	1389	1388	1387	1386	1385	1384	1383	1382	1381	1380	1379	1378	1377	1376	1375	1374	1373	1372	1371	1370	1369	1368	1367	1366	1365	1364	1363	1362	1361	1360	1359	1358	1357	1356	1355	1354	1353	1352	1351	1350	1349	1348	1347	1346	1345	1344	1343	1342	1341	1340	1339	1338	1337	1336	1335	1334	1333	1332	1331	1330	1329	1328	1327	1326	1325	1324	1323	1322	1321	1320	1319	1318	1317	1316	1315	1314	1313	1312	1311	1310	1309	1308	1307	1306	1305	1304	1303	1302	1301	1300	1299	1298	1297	1296	1295	1294	1293	1292	1291	1290	1289	1288	1287	1286	1285	1284	1283	1282	1281	1280	1279	1278	1277	1276	1275	1274	1273	1272	1271	1270	1269	1268	1267	1266	1265	1264	1263	1262	1261	1260	1259	1258	1257	1256	1255	1254	1253	1252	1251	1250	1249	1248	1247	1246	1245	1244	1243	1242	1241	1240	1239	1238	1237	1236	1235	1234	1233	1232	1231	1230	1229	1228	1227	1226	1225	1224	1223	1222	1221	1220	1219	1218	1217	1216	1215	1214	1213	1212	1211	1210	1209	1208	1207	1206	1205	1204	1203	1202	1201	1200	1199	1198	1197	1196	1195	1194	1193	1192	1191	1190	1189	1188	1187	1186	1185	1184	1183	1182	1181	1180	1179	1178	1177	1176	1175	1174	1173	1172	1171	1170	1169	1168	1167	1166	1165	1164	1163	1162	1161	1160	1159	1158	1157	1156	1155	1154	1153	1152	1151	1150	1149	1148	1147	1146	1145	1144	1143	1142	1141	1140	1139	1138	1137	1136	1135	1134	1133	1132	1131	1130	1129	1128	1127	1126	1125	1124	1123	1122	1121	1120	1119	1118	1117	1116	1115	1114	1113	1112	1111	1110	1109	1108	1107	1106	1105	1104	1103	1102	1101	1100	1099	1098	1097	1096	1095	1094	1093	1092	1091	1090	1089	1088	1087	1086	1085	1084	1083	1082	1081	1080	1079	1078	1077	1076	1075	1074	1073	1072	1071	1070	1069	1068	1067	1066	1065	1064	1063	1062	1061	1060	1059	1058	1057	1056	1055	1054	1053	1052	1051	1050	1049	1048	1047	1046	1045	1044	1043	1042	1041	1040	1039	1038	1037	1036	1035	1034	1033	1032	1031	1030	1029	1028	1027	1026	1025	1024	1023	1022	1021	1020	1019	1018	1017	1016	1015	1014	1013	1012	1011	1010	1009	1008	1007	1006	1005	1004	1003	1002	1001	1000	999	998	997	996	995	994	993	992	991	990	989	988	987	986	985	984	983	982	981	980	979	978	977	976	975	974	973	972	971	970	969	968	967	966	965	964	963	962	961	960	959	958	957	956	955	954	953	952	951	950	949	948	947	946	945	944	943	942	941	940	939	938	937	936	935	934	933	932	931	930	929	928	927	926	925	924	923	922	921	920	919	918	917	916	915	914	913	912	911	910	909	908	907	906	905	904	903	902	901	900	899	898	897	896	895	894	893	892	891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BANK OF CANADA

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1. ORIGINAL CONCEPTIONS OF THE BANK OF CANADA

1. The previous Royal Commission in Canada, comparable to the one now sitting was the Royal Commission on Banking and Currency in Canada, which, under the Chairmanship of Lord Macmillan, held hearings and made its Report in 1933. It is appropriate to review briefly the scope of its findings which were principally related to:

i. The provisions of the Bank Act, in the light of the forthcoming 1934 revision.

ii. The facilities provided by the Finance Act of 1923.

iii. The advisability (or otherwise) of establishing a central bank with special reference to such a bank's relationship with existing commercial banks, its authority and its functions.

2. The Report related how the Canadian banking system had evolved over a long period of years in such a manner as to suit the peculiar needs of the country. However, with the changes in the economy that had taken place since the Great War, the system was not as satisfactory, relatively, as it had been. Some of these changes included the extensive need for foreign borrowing to finance the country's development, difficulties of making payment of both principal and interest on such debt, and some degree of economic instability caused by the greater dependence of Canada

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1 upon world economic conditions and prices resulting
2 from an increasing volume of both exports and imports.

3 3. Internally, there was also a certain lack
4 of flexibility under the terms of the Finance Act, which
5 permitted the banks to obtain advances from the Treasury
6 Board against suitable collateral. (Rates, terms,
7 amounts and margins on such advances were determined by
8 the Board which was comprised of the Minister of Finance
9 and several Cabinet Ministers and was, thus, purely
10 political. The rate at the time of the hearings was
11 $2\frac{1}{2}$ per cent, which became the initial level of the Bank
12 of Canada's discount rate.) Advances were frequent,
13 since they were an important means of the banks maintaining
14 adequate cash ratios in the face of seasonal variations
15 in economic activity and loan demand. Another method
16 was the use of the New York money market where "secondary"
17 reserves could be employed profitably.

18 4. There was no single banking authority
19 which was detached from commercial banking and yet
20 linked to national business which could endeavour to:

- 21 1. Maintain stability in the currency
22 and price level.
- 23 ii. Regulate the quantity and flow of
24 credit, seasonal or otherwise.
- 25 iii. Regulate exchange fluctuations arising
26 from trade and capital flows.
- 27 iv. Co-operate in international monetary
28 affairs with other governments and
29 central banks.
- 30 v. Provide impartial and sound advice on
internal fiscal policy.

upon world economic conditions and prices resulting from an increasing volume of both exports and imports.

3. Interest, there was also a certain lack of flexibility under the terms of the Finance Act, which permitted the banks to obtain advances from the Treasury Board against suitable collateral. (Hence, terms, amounts and margins on such advances were determined by the Board which was comprised of the Minister of Finance and several Cabinet Ministers and was, thus, purely political. The rate at the time of the hearings was 2½ per cent, which became the initial level of the Bank of Canada's discount rate.) Advances were frequent, since they were an important means of the banks maintaining adequate cash ratios in the face of seasonal variations in economic activity and loan demand. Another method was the use of the New York money market where "secondary reserves could be employed profitably.

4. There was no single banking authority which was detached from commercial banking and yet linked to national business which could endeavour to:

- i. Maintain stability in the currency and price level.
- ii. Regulate the quantity and flow of credit, seasonal or otherwise.
- iii. Operate in international monetary affairs with other governments and



5. Experience in other countries indicated that a central bank could perform all of these functions. Indeed, since it appeared that no other body could do so, the Commission (by a majority) recommended the establishment of such a bank.

6. The Commission felt that the Bank should be free from political interference (Macmillan Report - paragraph 219. See Exhibit 1.) and, as such, should not be a direct organ of the government. However, the government should have some control over the appointment of the senior officers and directors, all of whom should have experience, skill and integrity in order that the bank could gain the confidence of the Government, the public, the "commercial" banks and its counterparts abroad. The feeling was that the share capital should be subscribed by the general public, with dividends limited to a nominal amount, and any other profits accruing to the government. Other recommendations provided that the new Bank should:

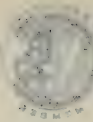
i. Have the sole right of note issue.

ii. Be banker to the Dominion government.

iii. Hold deposits of each of the commercial banks. (The suggested rate was 5 per cent of each bank's deposit liabilities. This was incorporated in amendments to the Bank Act in 1934).

iv. Buy and sell exchange and specified securities, as well as discounting the latter.

v. Issue and manage the public debt of the government.



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1 On this last function, comments were so limited that one
2 may conclude that the Commission had not visualized the
3 future magnitude of the job and the obvious conflict
4 of interest with monetary policy which was later to
5 materialize. On the other hand, the Report went to
6 considerable length in describing the central bank's
7 other functions, such as exchange dealing and monetary
8 policy, its effects upon the level of economic activity,
9 ways and means by which commercial banks' reserves could
10 be changed, etc. The Commission expressed the view
11 that in Canada, despite the absence of a money market,
12 the banking system would be sufficiently sensitive to
13 changes in the discount rate, open-market and foreign
14 exchange operations, for the central bank to be able to
15 initiate or counteract trends as circumstances required.
16 The Report also pointed out that central bank control
17 over exchange rates was desirable, since fluctuations
18 were often the outcome of credit conditions which could
19 cause short term capital movements, extensive foreign
20 borrowing or lending, and because internal price levels,
21 to the extent they were influenced by changing credit
22 conditions, could vary the volume of international
23 trade. (MacMillan Report - paragraphs 206-210, 218,
24 229-230. See Exhibit 2). (In passing, and as a matter of
25 interest, the Commission felt that the provision in the
26 Bank Act limiting the rate of interest which the
27 commercial banks could charge should be repealed. In
28 those days, the maximum rate was 7 per cent. The problem
29 is still with us and continues to limit the flexibility of
30 rates charged by the banks).



II. POSITION OF THE BANK OF CANADA

7. The provisions of the Act in 1934 which established the Bank of Canada followed quite closely the suggestions of the Macmillan Report. (Bank of Canada Report of the First Annual General Meeting of Shareholders February 25, 1936, page 11. See Exhibit 3). Particularly was this the case, with regard to public ownership and the concept that Bank policy was subject to Parliament. However, several steps including partial and ultimately complete nationalization, more government control over Board appointments and the limiting of the Governor's power of veto over Board decisions, changed the original basic concept of the Bank's position and made it responsible to the government of the day (rather than to parliament) and also set out that the Bank should operate in such a way to implement that government's policy. (Several important statements have been made clarifying this matter, among them, that by the Honourable J.L. Ilesley in 1941, with subsequent remarks by G.F. Towers in 1954 and by J.E. Coyne in 1956. Shortly after his appointment as Governor of the Bank of Canada in 1961, Louis Rasminsky echoed these earlier views. See Exhibit 4). Thus, while it became established that the Bank has freedom in formulating its policy, such policy must be in agreement with that of the Government. In other words, the Bank should have discretion in effecting policy, and the government should have no power to change the methods being used. For this system to function, there are three basic assumptions:



i. The government's policy must be reasonable and sound and not dictated by political aims.

ii. Both the Bank and its Governor must be held in high esteem and their prestige unquestioned, and

iii. There must be the closest of liaison and co-operation between the Government and the Bank.

The unhappy events in 1961 indicate the unfortunate possibilities when any one of these prerequisites is missing. To avoid a repetition of last year's happenings which lowered the prestige of both Canada and its Central Bank, it is suggested that some formal and dignified procedure should be established in the event that there are further disagreements on fiscal or monetary policy between Government and Governor which cannot be resolved. Mr. Rasminsky has suggested the desirability of legislative changes in the Bank of Canada Act to deal with this situation. (Louis Rasminsky, Statement July 31, 1961). This seems to make sense in the light of uncertainties created by the Honourable Donald M. Fleming who stated: "...the government would have no power whatever to terminate the terms of office of the directors or the governor, (House of Commons, February 21, 1961). and in a matter of a few months demanded Governor Coyne's resignation.

III. BANK OF CANADA AND DEBT MANAGEMENT

8. While the original Bank of Canada Act (1934) provided for the Bank to act as the government's

reasonable and sound and not

dictated by political aims.

ii. Both the Bank and the Governor must

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demanded Governor Goyne's resignation.

8. While the original Bank of Canada Act



1 agent "in the payment of interest and principal and
2 generally in respect to management of public debt in
3 Canada", it, in fact, did not become the government's
4 agent until 1938. (Report of the Governor of the Bank
5 of Canada to the Minister of Finance for 1938, page 9.
6 See Exhibit 5) This was accomplished by the Loans and
7 Interest Branch of the Department of Finance being
8 transferred to the Bank and called The Public Debt
9 Division. It was thought at the time that this would
10 ensure closer liaison between the Bank and the Department
11 of Finance and that any conflicts might be more easily
12 resolved. Since the objectives of the Bank, as set out
13 in the preamble to the Bank of Canada Act were ".....
14 to regulate credit and currency in the best interests
15 of the economic life of the nation, to control and
16 protect the external value of the national monetary unit
17 and to mitigate by its influence fluctuations in the
18 general level of production, trade, prices and employment,
19 so far as may be possible within the scope of monetary
20 action, and generally to promote the economic and
21 financial welfare of the Dominion.....", and these
22 clearly should be the objectives of government, no
23 serious difficulties were envisaged which would cause
24 fiscal policy and its resultant debt management problems
25 to take precedence over the Bank's monetary policy, which,
26 after all, was presumably, also in everyone's best
27 interests. However, years of war and preparedness for
28 was, together with the growth of the welfare state
29 concept have resulted in a most troublesome conflict of
30 interest position for the Bank of Canada in implementing



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1 its policy, and at the same time having to raise enormous
2 amounts of money for the government. Since it is evident
3 that the Government cannot be denied its cash require-
4 ments, the basic objectives of sound monetary policy,
5 even combating inflation, have been, from time to time,
6 sacrificed or delayed. It appears that debt
7 management should revert to the Department of Finance,
8 since in this way not only the Department, but the
9 Cabinet as a whole, may be made more aware of the problems
10 of the fiscal policy being followed.

11 9. While maintaining that debt management
12 should revert to the Department of Finance, it is
13 relevant to make reference to some of the methods used
14 by the Bank of Canada since it took over the function in
15 1938. Normally, in public issues, the Bank contacts
16 its list of primary distributors which includes the
17 chartered banks, most of the members of the I.D.A.C.,
18 stock brokers and others, and is believed to number
19 between 250 and 300. It may properly be contended that
20 this list is too big and unwieldy to be efficient, and
21 that it should be reduced to those organizations which
22 normally position and make markets in government
23 securities. Other dealers, brokers, or agents could
24 apply for bonds (when they have a demand for them) to
25 this group on a split underwriting fee basis. There
26 follows an outline of some of the methods which have been
27 used to place issues:

- 28 i. The Bank has purchased entire
29 issues directly from the Government
30 for cash, e.g. Treasury notes

the policy, and the Government is not in a position to
amounts of money for the Government. Since it is evident
that the Government cannot be denied the cash require-
ments, the basic objectives of sound monetary policy,
with monetary stability, have been given the first
priority. It appears that debt
management should revert to the Department of Finance,
since in this way not only the Department, but the
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should revert to the Department of Finance, it is
relevant to make reference to some of the methods used
of the Bank of Canada since it took over the function in
this regard. It is noted that the list of primary distributors which includes the
stock brokers and others, and is believed to number
between 250 and 300. It may properly be contended that
this list is too big and unlikely to be efficient, and
that it should be reduced to those organizations which
normally position and make markets in Government
securities. It is suggested that the list be reduced to
apply for bonds (when they have a demand for them) to
this group on a split underwriting fee basis. There
follows an outline of some of the methods which have been
used to place issues:

1. The Bank has purchased securities
issued directly from the Government



1 during wartime.

2 ii. The Bank has negotiated on behalf
3 of the government with the chartered
4 banks for the placement, on a formula
5 basis, of illiquid low-yielding
6 deposit certificates. This was
7 also done in wartime, and again
8 to finance exchange flows around
9 1950, at which time the banks
10 objected on the grounds that
11 "forced" lending at low interest
12 rates was involved.

13 iii. The Bank has conducted regular auctions
14 of treasury bills. The Annual Report
15 of the Governor of the Bank for 1956
16 described the method used. Basically,
17 bills have not been used to any
18 major extent as a method of raising
19 money for the Government, but as a
20 liquidity instrument through which
21 the banks could adjust their reserves
22 with a minimum of difficulty and as an
23 aid in the development of a money
24 market. Increases in 91-day bill
25 outstandings and the issuance of bills
26 with terms of six months, nine months,
27 and one year have taken place as bank
28 assets grew and the money market
29 developed, although some observers
30 now feel that secondary reserves at



11. The Bank has negotiated on behalf of the government with the chartered banks for the placement, on a formula basis, of 11-1/2% low-yielding deposit certificates. This was also done in wartime, and again to finance exchange flows around 1950, at which time the banks objected on the grounds that "forced" lending at low interest

11A. The Bank has conducted regular auctions of treasury bills. The Annual Report of the Governor of the Bank for 1956 has stated that the use of treasury bills have not been used to any major extent as a method of raising money for the Government, but as a financial instrument through which the banks could raise their reserves with a minimum of difficulty and as an aid in the development of a money market. Increases in 91-day bill outstanding and the issuance of bills with terms of six months, nine months, and one year have taken place as bank assets grew and the money market developed, although some observers



1 the banks contain an element
2 of forced lending. It has been
3 suggested that consideration might
4 be given, in the interests of
5 convenience on smaller orders to
6 allotting amounts up to a specified
7 maximum, in full at the average
8 award, as is the practice in the
9 United States, (R.V. Roosa, Federal
10 Reserve Operations in the Money and
11 Government Securities Markets, page
12 38. See Exhibit 6) at the weekly
13 auctions.

14 iv. Occasionally, the Bank has placed
15 with the banks short-term marketable
16 issues, the proceeds of which have
17 tided over the government temporarily,
18 and have been retired from the funds
19 raised through the sale of Canada
20 Savings Bonds, e.g. in 1954 and 1958.
21 Such issues, unlike deposit certificates,
22 have been priced to yield a fair
23 return and have been liquid in the
24 sense that they were saleable.

25 v. On various occasions, the Bank and
26 the Department of Finance have
27 recruited personnel from primary
28 distributors for exceptionally
29 large operations, such as the National
30 War Finance Committee for Victory



the banks contain an element of forced lending. It has been suggested that consideration might be given, in the interests of convenience on smaller orders to allotting amounts up to a specified maximum, in full at the average award, as is the practice in the United States, (R.V. House, Federal Reserve Operations in the Money and Government Securities Market, p. 38. See Exhibit C) at the weekly auctions.

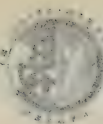
iv. Occasionally, the Bank has placed with the public short-term securities, the proceeds of which have been loaned over the government temporarily, and have been retired from the funds raised through the sale of Canada Savings Bonds, e.g. in 1954 and 1958. Such issues, unlike deposit certificates, have been placed to yield a fair return and have been liquid in the sense that they were saleable.

v. On various occasions, the Bank and the Department of Finance have recruited personnel from primary distributors for exceptionally large operations, such as the National



Loans, the Conversion Loan in 1958, and to some extent, the annual Canada Savings Bond campaigns. As a comment on this last, it appears that so much emphasis has been placed on their sale that difficulty is encountered by dealers in obtaining any material distribution of marketable bonds at retail. This is particularly so, since government bonds have been subjected to such wide price fluctuations. It is suggested that Canada Savings Bonds be used, as was the apparent original intent, as a means of saving, rather than an investment medium for funds already saved. (In his Report to the Minister of Finance for 1946, Mr. Towers stated: "The Canada Savings Bond was designed to incorporate those features of both Victory Bonds and War Savings Certificates most desired by individual savers. The chief purpose of its issue is to facilitate the continuance of regular personal savings habits developed in wartime.")

vi. Other methods used range from auctions to tap loans, including firm bonds to primary distributors, subscription privileges (which sometimes meant ordering ten or more times the par



loans, the Government Loan in 1958, and to some extent, the annual Canada Savings Bond campaign. As a comment on this last, it appears that so much emphasis has been placed on their sale that difficulty is encountered by dealers in obtaining any material distribution of marketable bonds at retail. This is particularly so, since government bonds have been subjected to such wide price fluctuations. It is suggested that Canada Savings Bonds be used, as was the apparent original intent, as a means of saving rather than an investment medium for funds already saved. (In his Report to the Minister of Finance for 1946, Mr. Towers stated: "The Canada Savings Bond was designed to incorporate those features of both Victory Bonds and War Savings Certificates most desired by individual savers. The chief purpose of its issue is to facilitate the continuance of regular personal savings habits developed in wartime.") Other methods used range from auctions to top loans, including firm bonds to primary distributions, subscription privileges (which sometimes meant



1 value of bonds required), acquisitions
2 of underwritings by the Bank and/or
3 government accounts either for cash
4 or in exchange for maturing or other
5 securities. It is unlikely that
6 the terms, pricing or amount of the
7 offering were discussed with primary
8 distributors, i.e. the organizations
9 and people who would be placing the
10 issue. Even at the time of offering,
11 there have been occasions when the
12 size of an issue has been unknown,
13 due to government or Bank subscriptions
14 which may or may not be re-offered
15 subsequently.

16 vii. Starting in 1961 and after the
17 government announced that it would
18 stay out of the long market to finance
19 its deficit, there have been some
20 changes in method. The pattern has
21 been about as follows: primary
22 distributors receive an offering of
23 firm bonds (participation determined
24 arbitrarily by the Bank and variable
25 from issue to issue) and usually may
26 order additional bonds, but not more
27 than twice the amount of firm bonds
28 accepted. This is an improvement
29 in that it eliminates some speculation.
30 (i.e. the order is perhaps four times



value of bonds required), and the
of underwriting by the Bank and/or
Government accounts either for cash
or in exchange for maturing or other
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Summary

vii. Starting in 1961 and after the
Government announced that it would
stay out of the long market for finance
the deficit, there have been some
changes in method. The pattern has
been about as follows: primary
distributors receive an offering of
the issue (primary distributors
explicitly by the Bank and various
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order additional bonds, but not more
than twice the amount of the bonds
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1 the amount which a primary
2 distributor expects to receive,
3 instead of say ten times or more)
4 It also enables the Minister of
5 Finance to continue to announce that
6 his financing was heavily over-
7 subscribed. (It is not recorded
8 whether the Minister, in making his
9 announcements, blushes with becoming
10 modesty or simply sighs with relief).
11 However, it precludes a distributor
12 from getting a materially larger
13 allotment because of the arbitrary
14 participation determined by the Bank,
15 even if orders have been received
16 in excess of such allotment. On the
17 other hand, if a distributor is unable
18 to (or does not, because he thinks
19 terms or pricing are not appropriate,
20 and being ethical, advises his clients
21 against the purchase of the security)
22 obtain sufficient orders to dispose
23 of the allotment, he must accept his
24 firm bonds and subscribe for additional
25 amounts, or run the risk of a reduced
26 participation in future financing, or
27 perhaps having his name deleted from
28 the Bank's list. Another undesirable
29 feature is that primarily, distributors
30 seldom can advise their customers



the amount which a primary distributor expects to receive, instead of say ten times or more. It also enables the Minister of Finance to continue to announce that his financing was heavily over-subscribed. (It is not recorded whether the Minister, in making his announcements, mixes with becoming modesty or simply sighs with relief.) However, it precludes a distributor from getting a materially larger allotment because of the arbitrary participation determined by the Bank, even if orders have been received in excess of such allotment. On the other hand, if a distributor is unable to (or does not, because he thinks terms or pricing are not appropriate, and being ethical, advises his clients against the purchase of the security) obtain sufficient orders to dispose of the allotment, he must accept his firm bonds and subscribe for additional amounts, or run the risk of a reduced participation in future issues, or perhaps having his name deleted from the Bank's list. Another undesirable feature is that primarily, distributors



1 properly as to the size of the issue
2 (since the Bank may also be a
3 subscriber and may or may not re-
4 offer) and hence the adequacy of the
5 pricing, from the point of view of
6 supply and demand factors, becomes
7 pure guesswork.

8 10. There have been four occasions (Sep./61,
9 Nov./61, Jan./62 and Apr./62) when the Bank has acquired
10 the entire amount of a new issue and there has been
11 national advertising thereof, mentioning all terms,
12 including par value, price, and yield in bold-face
13 type and below, in small print, the Bank's acquisition.
14 Subsequently, the Bank has re-offered the bonds to
15 primary distributors at or above the advertised price,
16 either for cash or in exchange for other securities.
17 Primary distributors are thus unable to obtain bonds
18 for clients at the advertised price and make a profit.

19 11. It should not be necessary to mention
20 that such methods of offering securities would be
21 unlikely to be approved by any Provincial Securities
22 Commission. Such clearance is, of course, unnecessary
23 for government offerings.

24 12. The above may sound like, but is not
25 intended to be, a condemnation of the Bank of Canada.
26 Rather, it is designed to point out that because of the
27 inadequacies of Canadian fiscal policy, and since it has
28 to be accepted that the Government-of-the-day must have
29 its cash requirements, the Bank, as the debt manager,
30 has become a victim of circumstances and has had to

properly as to the size of the issue

(since the Bank may also be a

subscriber and may or may not re-

offer) and hence the adequacy of the

pricing, from the point of view of

supply and demand factors, becomes

more important.

10. There have been four occasions (Sep.\61,

Nov.\61, Jan.\62 and Apr.\62) when the Bank has redrafted

the entire amount of a new issue and there has been

retention of advertising income, resulting in

including per value, price, and yield in bold-face

type and below, in small print, the Bank's explanation.

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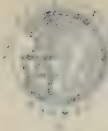
1 resort to any methods available to it to raise the money,
2 in the face of a growing and widespread distrust of
3 marketable Government of Canada long-term bonds as an
4 investment medium.

5 13. With debt management in the hands of the
6 Department of Finance, there is no reason why the Bank
7 would not continue to co-operate and provide impartial
8 and sound advice but the Department should, in addition,
9 recruit advisory committees from dealers, banks and
10 investing institutions, as is done in the United States.
11 The advice so obtained would reflect the state of capital
12 markets, investor demand for specified term categories
13 of bonds, coupons, yields, method of offering, etc.,
14 and would be the most ~~practical~~ and practical available.
15 It may even be considered desirable, in due course,
16 presuming a reasonable fiscal policy, to make use of
17 what has been the most successful method of borrowing
18 by others, i.e. negotiated transactions with dealer
19 syndicates. (See Exhibit 7). This method is described
20 in detail in Appendix "B" to this brief. Suffice to say
21 here that syndicate members with a liability in the
22 account would, generally speaking, be limited to those
23 organizations which are active in making trading markets
24 and which normally position government securities

25 IV. BANK OF CANADA FUNCTIONS

26 (1) General

27 143. Before outlining some of the tasks
28 available to the Bank to put its policy into effect,
29 it might be well to set out some of the problems which
30 such a policy is expected to reach.



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in detail in Appendix "B" to this paper. But it is not

here that syndicate members with a liability in the

account would, generally speaking, be limited to the

organizations which are active in making trading

and which normally position government securities

IV. THE DEPARTMENT OF FINANCE

(1) General

The Department of Finance is the central authority

for the management of the public debt and for the

issuance of government securities.

The Department is responsible for the management of the

public debt and for the issuance of government securities.

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public debt and for the issuance of government securities.



1 is to vary the level of the national income and prices,
2 up or down, as conditions indicate, through changes in
3 the chartered banks' cash positions. In order to keep
4 their ratios at the customary level, such variations will
5 tend to induce the banks to change their policies
6 regarding loans and/or investments which, in turn, will
7 change both the cost and availability of credit. Some
8 of these changes may be purely seasonal, (For example,
9 farm and grain loans, loans against Canada Savings Bonds
10 or heavier public demand for cash during holiday periods)
11 and because they tend to reverse themselves in due course
12 they seldom require more than temporary offsetting
13 action by the central bank, and since they are seasonal,
14 they can be anticipated and preparations can be made in
15 advance. There may also be temporary reasons for change
16 which cannot be anticipated and hence require more skill
17 in handling. Among these are substantial inward or
18 outward movements of capital, the government being
19 temporarily out of funds and, perhaps, on occasion in
20 recent years, the results of the Bank being a lender of
21 last resort to banks and money market dealers. Despite
22 the fact that these conditions are only temporary, they
23 may require quick offsetting action by the central bank
24 in order not to create conditions which would be
25 contrary to the monetary policy being pursued at the
26 time, nor to result in disorderly markets for exchange
27 or securities. Finally, there are situations which
28 require more permanent change, such as growth in
29 population and gross national product. In the initial
30 stages of such a trend, the banks can sell securities to



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up or down, as conditions indicate, through changes in
the chartered banks' cash positions. In order to keep
their ratios at the customary level, such variations will
tend to induce the banks to change their policies
regarding loans and/or investments which, in turn, will
change both the cost and availability of credit. Some
of these changes may be purely seasonal, (for example,
farm and grain loans, loans against Canada savings bonds
or heavier public demand for cash during holiday periods)
and because they tend to reverse themselves in the reverse
they seldom require more than temporary offsetting
action by the central bank, and since they are seasonal,
they can be anticipated and preparations can be made in
advance. There may also be temporary reasons for change
which cannot be anticipated and hence require more skill
in handling. Among these are substantial loans or
extended movements of capital, the government selling
temporarily out of funds and, perhaps, on occasion in
recent years, the results of the gold import and export
last resort to banks and money market dealers. Despite
the fact that these conditions are only temporary, they
may require either offsetting action by the central bank
in order not to create conditions which would be
contrary to the monetary policy being pursued at the
time, not to result in disorderly markets for exchange
or securities. Finally, there are situations which
require more permanent change, such as growth in
population and gross national product. In the initial



1 meet loan demand, and velocity of turnover may increase.
2 However, there are limits to both of these possibilities,
3 and in any case, if carried far enough, they might cause
4 the bond market to be seriously disrupted, making long-
5 term capital borrowing more costly or difficult. Under
6 such circumstances, the Bank must increase the cash
7 reserves of the chartered banks, or foreign borrowing
8 may increase to a point where exchange rates are
9 disrupted. Such changes in monetary policy require fine
10 judgment in order to ensure that productivity, and not
11 price, increases remain dominant. R.V. Roosa in his
12 pamphlet on Federal Reserve Operations, aptly refers to
13 these functions as "the defensive, avoiding mechanical
14 disturbances that could interfere with the smooth
15 functioning of the monetary system, and the dynamic,
16 using the potentialities of control over the reserve
17 base of a fractional reserve banking system to help
18 promote economic growth within a pattern of sustained
19 stability."

20 (11) Broadening the Government Securities Market

21 15. There is a situation which must be
22 improved by a central bank, or the tools at its disposal
23 will have limited impact, and that involves the
24 progressive broadening of the government securities
25 market. To increase the liquidity of the market, over
26 the years, the Bank of Canada has taken the initiative
27 with several steps and substantial progress has been made.
28 Regular treasury bill tenders were inaugurated in 1934,
29 culminating in weekly auctions in 1953, including those
30 for bills with terms longer than three months. During



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functioning of the monetary system, and the dynamic,
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(1) Evolving the Systematic Structure

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Regular Treasury bill tenders were inaugurated in 1934,
culminating in weekly auctions in 1953, including those
for bills with terms longer than three months. During



1 its existence, the Bank has always been available to the
2 chartered banks as a lender of last resort but it
3 started, in 1953, to make its discount window available
4 to selected dealers and did a substantial volume of short-
5 term purchase and resale agreement transactions with
6 them. (Report of the Governor of the Bank of Canada to
7 the Minister of Finance for 1953, page 8. See Exhibit
8 8) In 1954, changes in the Bank Act made possible,
9 for the first time, the real beginnings of a money
10 market (For a description of money market and its
11 functions see Standing Committee on Banking and Commerce,
12 March 16, 1954. See Exhibit 9) in Canada which, through
13 a more liquid bill market and the movement of day-to-day
14 borrowings by dealers, enabled the chartered banks
15 to adjust their cash without dealing directly with the
16 Bank of Canada, and also resulted in non-bank liquidity-
17 conscious investors becoming important holders of bills
18 and other short-term government securities. (Report of
19 the Governor of the Bank of Canada to the Minister of
20 Finance for 1954, pages 11-12. See Exhibit 10). From
21 time to time, the Bank has taken the initiative in
22 causing a reduction in the costs of handling securities,
23 through providing free and simultaneous out-of-town
24 transfers at its agency points, reduced over-
25 certification charges and free movement of day loans
26 within the banking system. (For a detailed analysis
27 see "Broadening the Money Market" by R.M. MacIntoch,
28 Canadian Banker, Autumn 1954). It has also from time
29 to time provided borrowing facilities in securities
30 through sale and repurchase agreements with dealers.



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conducting a valuation in the case of housing securities,
through providing free and simultaneous out-of-town
transfers at its agency points, reduced over-
certification charges and free movement of day loans
within the banking system. (For a detailed analysis
see "Broadening the Money Market" by R.H. MacInnes,
Canadian Banker, August 1954). It has also from time
to time provided detailed facilities in connection

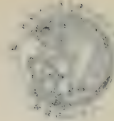


1 Obviously, the government market has been greatly
2 developed, making it more sensitive to supply and demand
3 factors and, therefore, to Bank of Canada action. (For
4 a description of the functions of a money market see
5 Chapter 7, "Foreign Central Banking, the Instruments of
6 Monetary Policy" by P.G. Fousek, which also describes
7 the broadening of the Canadian market. The London
8 and New York markets are described in "Federal Reserve
9 Operations in the Money and Government Securities
10 Markets" by R.V. Roosa. Both are publications of the
11 Federal Reserve Bank of New York).

12 16. Recently, discussions have been underway,
13 between the Bank of Canada and dealers, regarding a
14 market for bankers' acceptances. Another field to be
15 explored might be the extension of the Bank's lender
16 of last resort facilities to selected dealers, with
17 collateral being Canadas beyond the money market term
18 range of three years. This, with flexible, special,
19 call loans at realistic rates at the chartered banks
20 should in time broaden the market for mid and longer
21 term government bonds.

22 (iii) Statistical Material

23 17. The Bank has had success in other
24 directions. For example, its research department makes
25 excellent statistical material available, on a weekly
26 and monthly basis, which not only indicates the direction
27 of central bank activity but shows changing trends in
28 other segments of the economy. This material is
29 invaluable to business and all levels of government
30 in arriving at policy decision. If any criticism may be



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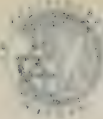
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1 cited in this respect, it would be in the lack of
2 explanatory or illustrative articles to complement the
3 bare statistics, other than the comments in the Annual
4 Reports of the Governor to the Minister of Finance
5 and occasional public addresses and parliamentary
6 hearings by Messrs. Towers and Coyne. (In the United
7 States, each of the twelve Federal Reserve Banks
8 publishes a monthly bulletin which contains articles
9 of national and local interest. In addition, the
10 Board of Governors of the Federal Reserve System has
11 monthly publications which are invaluable. All of these
12 contain articles, reproductions of speeches of senior
13 officers of the banks, etc., which enlarge on available
14 statistics. Each also has an annual report edition,
15 and periodically, informative booklets are published).
16 Such documentation would be most useful to educational
17 bodies, and would have facilitated the writing of this
18 appendix. (The Report of the Committee on the Working
19 of the Monetary System made similar recommendations
20 respecting the Bank of England and subsequently the
21 Bank's Central Banking Information Department has been
22 issuing a most informative Quarterly Bulletin. See
23 Exhibit 11). One mechanical recommendation would be
24 the publication of bond holdings of the Bank and the
25 chartered banks, in term categories of three years
26 and under and over three years, to conform to the terms
27 of reference on money market securities. Another would
28 be making available statistics indicative of overall
29 public liquidity, including holdings of commercial
30 paper and government (Federal, Provincial and Municipal)



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1 securities due in less than one year as well as publicly
2 held money supply and outstanding Savings Bonds.

3 V. BANK OF CANADA'S BOARD OF DIRECTORS

4 18. There is, however, one situation where there
5 appears to be room for improvement. The Macmillan Report
6 stated that it was vital that the management and Board
7 of Directors of the Bank should be filled by persons
8 with the highest degree of experience, skill and integrity.
9 (Macmillan Report - paragraph 227. See Exhibit 12). The
10 government does not seem to have been successful in
11 appointing to the Bank's Board people whose skill or
12 experience appear to qualify them to assist, materially,
13 the Governor and his senior personnel.

14 19. Working from the reports of the Bank of
15 Canada since its inception, there appears to have been
16 44 directors (excluding the Governors, the Senior Deputy
17 Governors and the Deputy Ministers of Finance) who have
18 served about 300 man-years. Little information is
19 available on some of them as to their "experience
20 and skill" in financial matters and several did not
21 appear in publications such as "Who's Who in Canada"
22 during their terms as directors. Adding together the
23 man-years served of those who are known to have been,
24 prior to, during, or subsequent to their terms of office,
25 investment dealers, stock brokers, officers or directors
26 of life insurance companies, officers or directors of
27 chartered banks, officers, directors or members of
28 advisory boards of trust companies or economists, the
29 total comes to about 125 (after eliminating duplications
30 in the above-mentioned categories). This is not to



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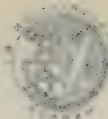
1. THE BANK OF CANADA

18. There is, however, one situation where there appears to be room for improvement. The Macmillan Report stated that it was vital that the management and Board of Directors of the Bank should be filled by persons with the highest degree of administrative ability and integrity. (Macmillan Report - paragraph 207, see Exhibit 12). The Government does not seem to have been successful in appointing to the Bank's Board people whose skills or experience appear to qualify them to assist, substantially, the Governor and his senior personnel.

19. Working from the reports of the Bank of Canada since its inception, there appears to have been 44 directors (excluding the Governor, the Senior Deputy Governor and the Deputy Ministers of Finance) who have served about 300 man-years. Little information is available on some of them as to their "experience and skill" in financial matters and several did not appear to qualify them as directors. Aiding together the man-years served of those who are known to have been, either as, during, or subsequent to their terms of office, investment dealers, stock brokers, officers or directors of life insurance companies, officers or directors of chartered banks, officers, directors or members of advisory boards of trust companies or economists, the total comes to about 125 (after eliminating duplications in the above mentioned categories). This is not to



1 question the integrity of, nor to belittle the advice
2 the others might have been able to provide to the
3 Governor on such matters as the crop outlook, conditions
4 in certain industries, etc., nor their political value.
5 However, considerably more than one-half of the man-years
6 served by outside directors of the Bank have been served
7 by men whose educational background and business
8 experience appears to have been non-financial. Steps
9 should be taken to remedy this deficiency and in any
10 case the selection of the directors should be based on
11 competence and qualifications and not on racial or
12 religious grounds, place of residence, political
13 affiliation or social position. (For a description of the
14 selection of directors of the Federal Reserve Banks, see
15 Chapter IV of The Federal Reserve System, Purposes and
16 Functions, 1961 edition. The Court of the Bank of
17 England is described in paragraphs 752-753 in the
18 Committee on the Working of the Monetary System Report.
19 The Bank of Canada Act, sections 5-14, indicates
20 management requirements of the Bank). An appropriate
21 Board of Directors would not only be helpful to the
22 senior officers of the Bank in their deliberations, but
23 would enhance the Bank's prestige and possibly create
24 an atmosphere of independence from government on policy
25 matters, because of their recognized intelligence and
26 importance in the business and financial spheres. In
27 the interests of providing the Governor with genuinely
28 useful guidance, it is suggested that a knowledgeable
29 Executive Committee be selected from the Board which
30 should meet frequently, possibly fortnightly, with the



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Составляя на том же уровне, сформулируйте

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[illegible]

as / 1967-68 for the smallholder and peasant

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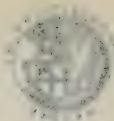
1 entire Board meeting at least once a month. In addition,
2 consideration should be given by the Bank to the
3 appointment of advisory committees, such as those
4 suggested for consultation with the Department of
5 Finance.

6 VI. BANK OF CANADA AND MONETARY POLICY

7 20. Most of the traditional tools of central
8 banking are available to the Bank of Canada. Some have
9 not been used and others have been, with wide variations
10 of success. Basically, the most important and
11 effective method of central bank control has been the
12 variation of bank reserves (expansion or contraction of
13 the money supply) and this may be accomplished in several
14 ways. This is so-called quantitative control:

15 (1) Open-market operations

16 21. Obviously, by buying or selling securities
17 the Bank can affect the deposits and hence the reserve
18 ratios of the chartered banks. (The effects of open-
19 market operations in a fractional reserve banking system
20 are described in: (1) The Federal Reserve System,
21 Purposes and Functions, 1961 edition, pages 20-23, and
22 (2) Memoranda and Tables re Bank of Canada given
23 before the Standing Committee on Banking and Commerce,
24 House of Commons 1939, pages 30-34). However, there
25 must be a market for securities for open-market
26 operations to be effective, and the Bank of Canada has
27 taken the initiative in broadening the market with
28 some success, as has been indicated above. In addition
29 to market operations, the Bank can have the same effect
30 on bank reserves at the weekly bill tender by buying



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1 more or less of the current issue than it holds of the
2 one which co-incidentally matures. Since Bank policy
3 should always be directed at stabilizing the economy,
4 its market operations should not cause disruptions in
5 the government market, (in the sense that violent
6 fluctuations can be avoided) since, it is, of course,
7 the key market and determines the rates at which lesser
8 credits may borrow. (It has become customary for
9 professional investors to establish a notional yield
10 differential between Canada bonds and those of lesser
11 credits. This yield spread varies from time to time for
12 many reasons, but always exists.) The Bank seems
13 consistently, over the years, to have under-estimated
14 the psychological effects of its market operations,
15 which periodically have created excessive speculation and
16 something resembling panic. After all, the Bank is the
17 largest single holder of Canadian government securities.
18 It does not hold them for investment purposes in the sense
19 that most investors, such as chartered banks, insurance
20 companies, pension funds, trust companies or individuals
21 do, i.e. for security, liquidity or income. The Bank's
22 investments are held so that it can change the liquidity
23 or income. The Bank's investments are held so that it
24 can change the liquidity position of others (or as a
25 result of having made such changes). Thus, the effects
26 of its market operations have a tremendous psychological,
27 as well as an actual impact on investors in general,
28 necessitating great deftness and skill in handling if
29 makets are not to be disturbed.

30 22. For many years, the Bank of Canada has



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1 operated in all term segments of the market. Mr. Towers
2 (Standing Committee on Banking and Commerce, March 18,
3 1954. See Exhibit 13) explained that trading in longer-
4 term government was designed to broaden the market and
5 he expressed the hope that the Bank could in future play
6 a smaller part, as dealers expanded their operations.
7 Mr. Coyne (Standing Committee on Banking and Commerce,
8 May 15, 1956. See Exhibit 14) pointed out some of the
9 circumstances under which the Bank bought and sold
10 securities. His statement seemed to suggest that the
11 Bank preferred to operate as a result of dealers
12 initiating the selling or buying or if it became necessary
13 to mitigate fluctuations. The Radcliffe Committee's
14 Report (Report of the Committee on the Working of the
15 Monetary System, paragraphs 339, 340, 373. See Exhibit
16 15) indicated that the Bank of England should operate in
17 longer issues to prevent disorderly markets and if it
18 became desirable to change the liquidity position of the
19 "private sector". Stress is on operations in the bill
20 market, as far as money management is concerned. (Foreign
21 Central Banking: The Instruments of Monetary Policy -
22 Fousek - pages 34-35. See Exhibit 16). W.W. Riefler
23 (Open Market Operations in Long-Term Securities -
24 Federal Reserve Bulletin, November 1958, page 1260.
25 This article should be read in its entirety) described
26 the policy of the Federal Reserve System in its market
27 operations since 1953 and concluded that, since buying
28 or selling bills had the same effect in varying bank cash
29 as trade in any other segment of the market, a bills
30 only (or preferably) policy was justified. Furthermore,



1 operating in longer bonds tended to widen their price
2 fluctuations from cycle to cycle and was not justified,
3 except to smooth out disorderly markets. Mr. Riefler's
4 concluding remarks were as follows:

5 23. "The decision of the Federal Open Market
6 Committee in 1953 to confine open market operations to
7 short-term issues reflected primarily realization that
8 the Government securities market occupied a crucial
9 position in the postwar financial structure and a desire
10 to promote the better technical functioning of that
11 market by minimizing disturbances that might result from
12 the System's own operations. Since the bill sector was
13 very much broader than any other sector of the market, it
14 was clear that such disturbances would be held to a
15 minimum if System operations were confined primarily to
16 bills. The decision of the Committee reflected its
17 confidence that confining operations to the shortest
18 term securities would improve and not impair the market
19 effectiveness of Federal Reserve policy actions.

20 24. "Basically, the System aids the economy in
21 times of recession by increasing flows of loanable funds
22 and thus helping to finance active demands in the markets
23 for men and materials. This is the ultimate aim of
24 monetary policy at such a time. The achievement of lower
25 interest rates in these circumstances represents a means
26 to an end, not an end in itself. The effective monetary
27 stimulant to the economy in time of recession is an
28 increase in the availability of reserves to the member
29 banks, since such reserves increase by a multiple factor
30 the supply of funds available for loans and investments



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1 and also help to create a financial environment in which
2 additional credit-worthy enterprises are both tempted
3 and able to borrow. This stimulant can be provided just
4 as effectively by operations in bills as by operations
5 in bonds.

6 25. "Conversely, the System acts to restrain
7 over-ebullience in the economy when it decreases the
8 rate of credit creation at the commercial banks, thus
9 minimizing excess pressure on the markets for goods and
10 labour. The relief of this pressure, not higher interest
11 rates, long- or short-term, is the object of a policy
12 of restraint. The effect of such restraint in the face
13 of active demands for credit will, of course, take the
14 form of higher interest rates which will help to bring
15 total money demand into line with resource availability.
16 When open market operations are used, it is the lessened
17 availability of bank reserves that effectuates this
18 restraint, not the fact that the security sold in
19 conducting the operation was a long-term bond. Sales of
20 bills are fully as effective in absorbing reserves from
21 the member banks as sales of long-term bonds. More
22 important, they minimize the risk of creating a
23 condition of disorder in the securities market, which
24 might force intervention by the System to support the
25 market at a time when broader economic considerations
26 called for restraint.

27 26. "The difficult problem for the System in
28 periods of recession or boom is to diagnose the state of
29 the economy and particularly the tempo of the money and
30 capital markets through which policy actions influence



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in bonds.

25. "Conversely, the System acts to restrain
over-ebullience in the economy when it decreases the
rate of credit creation at the commercial banks, thus
minimizing excess pressure on the markets for goods and
labour. The relief of this pressure, not higher interest
rates, long- or short-term, is the object of a policy
of restraint. The effect of such restraint in the face
of active demands for credit will, of course, take the
form of higher interest rates which will help to bring
total money demand into line with resource availability.
When open market operations are used, it is the loaned
availability of bank reserves that effectuates this
restraint, not the fact that the security sold in
conducting the operation was a long-term bond. This is
true as far as the effect on the money market is concerned.
The member banks as sales of long-term bonds. More
important, they minimize the risk of creating a
condition of disorder in the securities market, which
might force intervention by the System to support the
market at a time when broader economic considerations
called for restraint.

26. "The difficult problem for the System in
periods of recession or boom is to diagnose the state of
the economy and particularly the tempo of the money and



1 economic activity. The System must at all times act on
2 a judgment as to the volume of reserves that is most
3 appropriate to sustained economic growth and stability.
4 The formation of such a judgment involves a process of
5 continuous evaluation in which the System is always, in
6 a sense, probing the unknown and feeling its way.

7 27. "The difficulty of deciding on the
8 appropriate volume of reserves is magnified when the
9 most relevant indicators of conditions in the long-term
10 capital markets are deflected by transient or short-run
11 responses to the System's own operations. It is minimized
12 when the System is able to effectuate changes in the
13 reserve position of the banks through operations that
14 cause little if any immediate change in expectations,
15 particularly unjustified expectations with respect to
16 long-term yields. The outstanding advantage of open
17 market operations confined to short-term securities is
18 that they meet this criterion." W.C. Martin (Federal
19 Reserve Bulletin, March 1961, page 272. This statement
20 before the Joint Economic Committee should be read in its
21 entirety) confirmed the desirability of the Fed
22 staying in the short market, but in 1961 the outflow of
23 funds in the face of a need for easy credit caused it
24 to adopt a policy of buying longer securities to enlarge
25 bank cash. (operation nudge) Mr. Martin described these
26 operations in January, 1962 (Federal Reserve Bulletin,
27 February 1962, page 131. This statement before the
28 Joint Economic Committee should also be read in its
29 entirety) and implied some concern over the high
30 proportion of trading done by the Fed, particularly in



1 bonds due in more than ten years. Mr. J.L. Robertson,
2 of the Board of Governors of the Federal Reserve System,
3 urged that operations beyond the short term area be
4 terminated immediately in a dissent to the December 19,
5 1961 directive to the Federal Reserve Bank of New York.
6 (Annual Report of the Board of Governors of the Federal
7 Reserve System 1961 summarized the basis of Mr.
8 Robertson's dissent. Pages 97-98. See Exhibit 17).

9 28. The framers of the original Bank of
10 Canada Act (1934) apparently did not recognize any great
11 necessity for the Bank's market operations to extend
12 beyond bonds due in less than two years, since its
13 holdings of longer bonds (including provincials) were
14 limited to three times its paid-up capital or \$15
15 million. There have been several amendments to this
16 proviso, but even in 1954, prior to the amendment which
17 removed all such restrictions, holdings of bonds maturing
18 in more than ten years were limited to \$75 million.
19 (Holdings of bonds due in over ten years, as of July 31,
20 1954, were \$33 million and as of December 31, 1961, were
21 \$1,186 million. Month-end high was \$1,351 million in
22 June 1959. A major part of this increase was brought
23 about by the Conversion Loan of 1958). Since treasury
24 bills appear to have been created to be used as a
25 liquidity instrument, the weight of evidence seems to
26 indicate that the Bank of Canada should conduct its
27 open-market operations within the defined money market
28 range (maturities of three years or less), with some
29 emphasis on bills "preferably", excepting during periods
30 of crisis when the orderly market (Committee on the



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of the Board of Governors of the Federal Reserve Bank,
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range (maturities of three years or less), with some



1 Working of the Monetary System Report, paragraph 551,
2 See Exhibit 18, and Federal Reserve Bank of Philadelphia,
3 1954, "Quest for Stability", pages 18-19. See Exhibit
4 19.) concept should properly prevail in all term
5 categories.

6 29. There is a further matter concerning
7 open-market operations in Canada to be considered.
8 While recognizing the necessity for the Bank's Head
9 Office and senior officials being located in Ottawa,
10 trading markets are, in fact, in Toronto and Montreal,
11 and yet the Bank's trading desks in these cities are
12 understaffed and the traders are not given sufficient
13 authority to deal at their discretion. (This problem
14 of liaison seems to have received more recognition in
15 the United States, R.V. Roosa, Federal Reserve Operations,
16 pages 94-95. See Exhibit 20). Not only does this slow
17 down trading, (Inability to deal over the telephone
18 tends to create apprehension and from time to time
19 leads to speculation and larger offerings or bids than
20 exists from business on hand), but the traders have
21 insufficient time to discuss market conditions,
22 expectations, etc. with the dealers in order to get the
23 "feel" of the market and sometimes this is more
24 important than technical projections of probabilities.
25 This could mean that those, in Ottawa, on whom the
26 responsibility for policy decisions rests, may not be
27 close enough to the market to make appropriate judgments.
28 Enlarging the staff of the trading departments in the
29 two principal trading centres seems to be indicated.

30 30. The Bank has another trading problem, since



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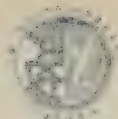


1 it stands ready to deal with all of its primary
2 distributors from coast to coast. In recognition of
3 this problem it has, in effect, eliminated many of these
4 dealers by setting minimum amounts (\$250,000 in bills
5 and Canadas due within three years and \$100,000 in
6 longer bonds) in which it will deal. By way of
7 simplification, consideration might be given to limiting
8 trading to those organizations which endeavour to make
9 markets, and which would, then, become jobbers for all
10 other dealers.

11 (ii) Operation of Government Accounts

12 31. Since the Bank of Canada is the
13 Government's banker, it holds in the Receiver General's
14 Account some of the Government's cash, the balance being
15 on deposit with the chartered banks. The proportion
16 held by the Bank may be varied resulting in "draw downs"
17 (decreases in cash) or "re-deposits" (increase in cash)
18 for the chartered banks, both of which alter their cash
19 ratios. The Government has other accounts for which the
20 Bank acts as agent and changes in their holdings may also
21 alter the chartered banks' cash positions. Among these
22 accounts are:

23 32. The Securities Investment Account, which
24 is used to invest surplus government cash, acquisition
25 of bonds for cancellation, purchase of external-pay bonds
26 when exchange rates are favourable, etc. According to
27 a press release from the office of the Minister of
28 Finance, dated November 8, 1961, certain holdings of
29 government bonds in the account, totalling some \$82
30 million, were cancelled. (A further \$37 millions were



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Government bonds in the account, totalling some \$82



1 cancelled as of March 31, 1962). This had at the time
2 bullish implications for bond prices, since these bonds
3 could have been sold in the market when the government
4 required cash. Instead, it chose to raise new money
5 in one of its frequent cash borrowings in the short end
6 of the market. Another type of use to which the account
7 has been put took place in February of both 1961 and 1962.
8 On these occasions, the account acquired, temporarily,
9 bonds on a purchase and resale basis from the Bank of
10 Canada, in order to reduce seasonally expanded chartered
11 bank cash without open-market sales which might have
12 disturbed the market and would have had to have been
13 reversed in any case.

14 33. The Unemployment Insurance Fund which,
15 due to portfolio changes adopted in 1961, is no longer
16 the important factor it once was. (According to a
17 press release from the office of the Minister of Finance,
18 dated October 2, 1961, government bond holdings of the
19 Fund, totalling \$201 million, were cancelled and replaced,
20 after repayment of advances from the Treasury, with non-
21 marketable redeemable 3 3/4 per cent bonds). Actually,
22 its operation by the Bank in prior years was often
23 contrary to the Bank's monetary policy, e.g. in periods
24 of recession and unemployment, the Bank's policy
25 would normally be expansionary, and yet to put the
26 Fund in cash to meet its requirements, its holdings of
27 bonds had to be sold. Seasonal factors were also
28 upsetting from time to time.

29 34. The Purchase Fund (The Purchase Fund was
30 established by the June 20, 1961 Budget, House of



described as an "open market" operation. This was the first time the Federal Reserve had ever sold government securities in the open market. It was a "reverse" operation, in that it was designed to reduce the amount of cash in the banking system. Instead, it chose to raise new money by selling government securities. Another type of use to which the account has been put took place in February of both 1961 and 1960. In these instances, the account was used to purchase bonds on a purchase and resale basis from the Bank of Canada, in order to reduce seasonally expanded chartered bank cash without open-market sales which might have disturbed the market and would have had to have been reversed in any case.

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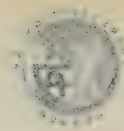
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34. The Purchase Fund (The Purchase Fund was



1 Commons. See Exhibit 21) will likely be used to acquire
2 mid and long-term bonds for cancellation, to influence
3 the yield structure and to stabilize the market. The
4 effect of this fund is similar to that of a sinking fund
5 and, as such, it should prove to be beneficial in time.
6 The periods of budgetary surplus, the use of the Fund
7 can result in retirement of debt in advance of maturity,
8 and the market level of certain term segments can be
9 influenced. However in deficit periods, it adds to the
10 cash borrowing requirements of the government and
11 involves the issuance of additional securities, presumably,
12 in a different term category. Thus, while one part of the
13 market may be supported, another could be adversely
14 effected. It may also be costly. (e.g. As of November
15 7, 1961, about \$61 million of securities held by the Fund
16 were cancelled. The average coupon on these securities
17 was 4.49 per cent and the average term to maturity $18\frac{1}{2}$
18 years. In September, 1961 the government issued 5-year
19 3-month $4\frac{1}{2}$'s ($4\frac{1}{2}$'s due December 15, 1966) to yield 4.66
20 per cent. On March 31, 1962, an additional \$105 million
21 was cancelled). It is not clear whether bonds acquired
22 and held in the Fund, but not yet cancelled, may be re-
23 offered for sale to the market. It seems apparent
24 that this should not be the case.

25 35. Evidence seems to indicate that on some
26 occasions the Bank's handling of transactions for these
27 accounts has left something to be desired. Whether the
28 fault lies with the Bank's periodic lack of feel for the
29 market, or the Department of Finance's decisions, or as
30 a result of having to operate, from time to time, in a



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1 manner contrary to intended monetary policy, is not
2 clear. However, one of the basic fundamentals of
3 successful bond trading is to complete transactions with
4 a minimum amount of disturbance to the market. Such has
5 not always been the case.

6 N.B. The cancellation, since Autumn 1961, of the
7 marketable bonds in the Securities Investment Fund,
8 the Unemployment Insurance Fund and the Purchase
9 Fund, totalling some \$486 million, has been
10 cynically referred to by some observers as
11 "reversing" the 1958 Conversion Loan.

12 36. Exchange Fund Account. Purchases or
13 sales of exchange, whether they be for the Bank's own
14 account or for the Exchange Fund Account, may tend to
15 contract, or enlarge, chartered bank reserves. However,
16 operations to vary reserves in this manner must be
17 harmonious with policy regarding exchange. Since 1952
18 (after the Foreign Exchange Control Board was abolished)
19 the Bank of Canada has operated the Fund for the
20 Government and, until recently, has apparently been
21 content to stabilize and maintain an orderly day-to-day
22 trading market, and to minimize wide fluctuations, while
23 letting the dollar find its own level. Canada's holdings
24 of gold and U.S. dollars were \$1,860 millions at the
25 end of 1952 and \$1,829 millions in 1960, which is
26 indicative of the relatively small over-all effect of the
27 operations. This may have been the result of the terms
28 of Canada's membership in The International Monetary
29 Fund which permitted an unpegged exchange rate, provided
30 the rate was not manipulated. Also, there appears to



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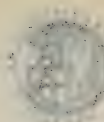
M.R. The same situation, since January 1961, of the convertible bonds in the Securities Investment Fund, the Unemployment Insurance Fund and the Purchase Fund, totalling some \$480 million, has been cynically referred to by some observers as "reversing" the 1958 Conversion Loan.

Exchange Fund Account

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1 have been the thought that the flow of foreign funds in
2 or out of Canada could be influenced more readily (and
3 perhaps more economically) by changing government bond
4 yields through monetary policy. (Hence, the close
5 attention paid to yield spreads between Canadian
6 government bonds and those of other countries,
7 particularly the United States). However, in 1961, the
8 government through avowed policy (House of Commons,
9 Budget Speech, June 20, 1961. See Exhibit 22) and
10 substantial operations in the exchange market,
11 definitely influenced, downward, the value of the
12 Canadian dollar in international markets. By the end of
13 1961, holdings of gold and U.S. dollars had risen to
14 \$2,056 millions, an increase of \$227 millions during
15 the year, despite a transfer to The International
16 Monetary Fund of \$50 million. In the first three
17 months of 1962 however pressures were in the opposite
18 direction and exchange holdings dropped by \$347 million.
19 (See Exhibit 23 for comments on exchange policy by W.
20 Earle McLaughlin at the Annual Meeting of the Royal
21 Bank of Canada January 11, 1962. The Honourable Donald
22 M. Fleming denied some of Mr. McLaughlin's allegations
23 in his Budget Speech on April 10, 1962. R.V. Roosa,
24 Under Secretary of the Treasury for Monetary Affairs
25 made some comments on exchange policy in an address
26 before the American Bankers Association in New York City
27 on February 7, 1962). Figures showing holdings of gold
28 and U.S. dollars are released monthly, which seemed
29 adequate prior to 1961. Since then, the swings have
30 been so large that the publication of weekly figures



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1 would be helpful.

2 37. In its trading of exchange, the Bank has
3 seldom operated in the futures market, despite the fact
4 that spot transactions may cause a maldistribution of
5 chartered bank cash or require offsetting action.
6 Since there are some seasonal movements of funds
7 internationally which tend to reverse themselves,
8 transactions in futures appear to be a simpler course.
9 Furthermore, international, short-run "hot" money flows
10 on a hedged basis, may be discouraged when such action
11 is deemed to be appropriate, by activity in the futures
12 market designed to alter the relationship to spot rates.
13 In view of our recently altered exchange policy, a full
14 examination of the situation seems to be desirable in
15 order to determine the adequacy (or otherwise) of our gold
16 and U.S. dollar reserves, our position vis-a-vis The
17 International Monetary Fund and the possible effects
18 on our balance of payments.

19 (iii) Regulation of chartered banks' cash
20 Reserves.

21 38. Cash reserves have traditionally become
22 considered to be the liquidity cushion enabling a bank
23 to meet its customers' demand for currency and to pay
24 cheques drawn by its depositors, i.e. they ensure adequate
25 liquidity in the banking system. The establishment of
26 a minimum cash ratio for the banks (whether it is varied
27 from time to time, or not) provides the basis from which
28 the central bank's open-market operations may secure their
29 intended results. (Bank Reserves, 1956 printing, page
30 10. Published by the Federal Reserve Bank of New York.

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the central bank's open-market operations and, hence, its

intended control of the money supply.



1 See Exhibit 24). This becomes evident, since it is
2 accepted that if a bank experiences difficulties in
3 maintaining its reserves at the required level, it is
4 obviously in an over-extended position and corrective
5 measures such as converting secondary reserves into
6 cash, calling loans, etc., become necessary.

7 39. Since 1954, the Bank of Canada has had the
8 power of varying the chartered banks legal cash ratio
9 between 8 per cent and 12 per cent of their deposit
10 liabilities, the change not to exceed one percentage point
11 at a time, and on one month's notice. The ratio was set
12 initially at 8 per cent and has not been changed. This
13 compares with a 5 per cent requirement previously
14 (calculated in a different way) and a 10 per cent rule
15 of thumb which had been maintained by the banks for many
16 years. The development of the money market, which
17 provided day loans and greater bill liquidity, enabled
18 the banks to work down from 10 per cent to close to 8
19 per cent. Mr. Towers felt that the Bank's power to alter
20 the cash ratio should be used only in some emergency,
21 such as when cash increases sharply under peculiar and
22 unavoidable conditions, and when off-setting action is
23 precluded or undesirable. (House of Commons - Standing
24 Committee on Banking and Commerce, March 18 and March
25 23, 1954. See Exhibit 25).

26 40. Late in 1955, the Bank induced the
27 chartered banks to "agree to endeavour to maintain",
28 in addition to their cash reserves of 8 per cent,
29 secondary reserves of 7 per cent of deposits, consisting
30 of cash, day loans or treasury bills, (Report of the



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39. Since 1954, the Bank of Canada has had the power of varying the chartered banks' legal cash ratio between 0 per cent and 12 per cent in 1 per cent increments. The legal cash ratio was set at a time, and on one month's notice. The ratio was set initially at 8 per cent and has not been changed. This compares with a 5 per cent requirement previously (calculated in a different way) and a 10 per cent rule of thumb which had been maintained by the banks for years. The development of the money market, which provided day loans and greater bill liquidity, enabled the banks to work down from 10 per cent to close to 8 per cent. Mr. Towers felt that the Bank's power to alter the cash ratio should be used only in some emergency, such as when cash increases sharply under peculiar and unavoidable conditions, and which is not a standing provision or undesirable. (House of Commons - Standing Committee on Banking and Commerce, March 18 and March 23, 1954. See Exhibit 25).

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Governor of the Bank of Canada to the Minister of Finance for 1955, pages 16-17. See Exhibit 26) a total of 15 per cent in all. This is not a legal requirement, but the banks are still living up to their "voluntary" agreement, despite their initial objections to it. The measure now seems to be of doubtful value (presuming that banks will continue to be reasonably cautious in their lending policies and desire satisfactory liquidity), since under tight credit conditions the banks may be willing to sell other less-liquid securities, i.e. mid and longer-term Canadas, in order to make loans, which could lead to a disorderly bond market, unless supported by the Bank, which would be contrary to intended policy. On the other hand, when the banks have excess liquidity above the 15 per cent, the requirement is ineffective in limiting credit. It may also be criticized on the grounds that it makes the banks a "captive" market for bills and, hence, the government could be accused of forced lending. (Excerpts from James Muir's address to the Annual Meeting of The Royal Bank of Canada, January 9, 1958. See Exhibit 27).

(iv) The Discount Rate

41. As the lender of last resort, a central bank usually establishes a minimum rate at which it will extend short-term advances against suitable collateral, to authorized bodies such as banks, which may require advances to replenish their reserves when some unexpected situation temporarily exhausts cash. Traditionally, the rate has been fixed and changes in it not only signal the expectations and intentions of the



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1 central bank, but also have led to changes throughout
2 the entire interest rate structure, i.e. credit tends to
3 become cheaper or more costly, as the case may be, as the
4 bank resists deflationary or inflationary pressures. If
5 used in conjunction with appropriate open-market
6 operations, both the availability and cost of credit tend
7 to be altered. As discount rate changes become under-
8 stood, they have a psychological (as well as an actual)
9 impact on investors, and thus, may tend to lessen the
10 extent of complementary open-market operations (or other
11 actions) necessary by the central bank to attain its
12 intentions. In Canada, little use of the Bank's
13 discounting facilities were made until 1953, when the
14 money market began to function. In 1954, a number of
15 investment dealers were given "lines of credit" with the
16 Bank and began using the discount window quite
17 extensively. Similar, but more official "lines" had been
18 given to the chartered banks many years previously.
19 (For comments on the Federal Reserve's discount window,
20 see pages 24-25, "Federal Reserve Operations in the
21 Money and Government Securities Markets, by R.V. Roosa.
22 See Exhibit 28). Several changes were made in the rate
23 during 1955-1956, but as of November 1, 1956, the Bank
24 announced that the rate would, in future, be permitted
25 to fluctuate each week at a level of 1/4 per cent higher
26 than the weekly average award on three-month treasury
27 bills. (See Exhibit 29 for dates and changes in the
28 discount rate, together with official comments in
29 connection therewith). As a surmise, one may ponder
30 whether the Governor felt that, since his efforts to



central bank, but also have led to changes in the
the active interest rate structure. The central bank
become cheaper or more costly, as the case may be, of the
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Bank and began using the discount window quite
extensively. Similar, but more official "lines" had been
given to the chartered banks many years previously.
(For comments on the central bank's discounting
the Bank's "discounting" facilities in the
early and government securities market, see R.V. Brown,
see Exhibit 10). Several changes were made in the rate
during 1955-1956, but as of November 1, 1956, the Bank
announced that the rate would, in future, be permitted
to fluctuate each week at a level of 1/4 per cent higher
than the weekly average award on three-month treasury
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connection therewith). As a surmise, one may ponder



1 contain credit in 1955-1956 had not been successful,
2 fiscal policy had taken precedence over monetary policy.
3 If so, he may also have felt that a much higher discount
4 rate might draw public attention to this dilemma.

5 42. The establishment of a "floating" rate
6 appears to have accomplished little -- indeed, it may have
7 hampered the Bank in implementing its policy since it is
8 generally recognized that the simultaneous use of more
9 than one tool by a central bank, e.g. open-market sales
10 in conjunction with an increase in the discount rate, is
11 helpful in attaining the desired result. Recently, too,
12 there have been examples in other countries of the use
13 of changed discount rates to influence the movement of
14 short-term capital between countries where such flows
15 were considered undesirable. Furthermore, the changes
16 in the fixed rate in 1955-1956 were beginning to have
17 effects on other interest rates (i.e. creating flexibility)
18 and the "disturbing" effects to business may have been
19 desirable under existing conditions of extraordinarily
20 high capital investment. There may be some justification
21 for the rate involving a penalty, (The banks are, in
22 effect, penalized by having to pay interest on advances
23 for seven days and yet receive a credit for only five,
24 in maintaining their cash ratios. Both the banks and
25 the dealers may have to pay a rate in excess of the
26 discount rate on renewals of advances, or use of advances
27 on more than one occasion during a calendar month. The
28 same applies on advances in excess of specified lines of
29 credit. In the case of dealers, lines of credit are
30 renewed or changed monthly and such changes may penalize



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1 a dealer by limiting his operations. On the other hand,
2 a Federal Open Market Committee directive, dated December
3 19, 1961, authorized the Federal Reserve Bank of New
4 York "to buy U.S. Government securities with maturities
5 of 24 months or less at the time of purchase....from non-
6 bank dealers...under agreements for re-purchase of such
7 securities.....in 15 calendar days or less, at rates
8 of not less than (a) the discount rate of the Federal
9 Reserve Bank of New York...or (b) the average issuing
10 rate on the most recent issue of 3-month Treasury bills,
11 whichever is the "lower". Under normal circumstances,
12 the applicable rate would be lower than the discount rate,
13 indicating that the penalty aspect is not considered to
14 be important. Annual Report of the Board of Governors of
15 the Federal Reserve System for 1961, page 92.) but the
16 $\frac{1}{4}$ per cent above current bill yields does not guarantee
17 such a penalty on all the securities which may be eligible
18 collateral for advances. However, minimizing the penalty
19 aspect has some merit since, from time to time, it may
20 enable money market dealers to carry substantial invent-
21 ories of short-term securities, thereby tending to
22 maintain a broad and active market. Some observers
23 have commented that if the floating rate were replaced
24 with an administered rate and the differential between
25 it and treasury bill yields widened significantly beyond
26 $\frac{1}{4}$ per cent, dealer willingness to carry large
27 inventories might be lessened which in turn might tend to
28 narrow the market. On the other hand, under these
29 circumstances, the Bank might like to see a smaller spread
30 with bill yields closer to the Bank rate. Since any



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1 validity a floating rate may have had in 1956 no longer
2 seems to exist, a return to an administered rate appears
3 to be desirable. (See Exhibit 30 for comments concerning
4 the discount rate by: James Muir - Annual Meetings of
5 The Royal Bank of Canada, January 9, 1958 and January
6 14, 1960, G. Arnold Hart - Annual Meeting of the Bank
7 of Montreal, December 5, 1960, J. Douglas Gibson -
8 Annual Meeting of The Bank of Nova Scotia, October 31,
9 1960, "Quest for Stability" Federal Reserve Bank of
10 Philadelphia, 1954). Any changes should be accompanied
11 by an explanatory statement from the Governor, and
12 supporting remarks by the Minister of Finance may be
13 appropriate on some occasions. By way of corroboration
14 of this suggestion, no other central bank in any country
15 in the world, with a money market, has adopted a
16 floating rate. (Mr. Rasminsky also implied doubts about
17 a floating rate in his 1961 Report by stating: ".....this
18 method of determining Bank rate has given rise to a good
19 deal of public discussion, and many and varied preferences
20 for alternative methods have been expressed.....I hope
21 and expect that the views of interested parties will be
22 made known in evidence before the Royal Commission and
23 it is my present intention to keep an open mind on the
24 matter until all those with a major interest in it have
25 had a chance to express their opinions.")

26 43. From time to time, one hears discussion of
27 a suggestion that rates against actual advances be set
28 so as to ensure the penalty aspect, with an accompanying
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1 take place. For the Bank of Canada to have dual rates
2 does not seem to make much sense, if it does not lend at
3 one of the rates. Indeed it might dilute the effective-
4 ness of the "signal" rate.

5 44. In all the quantitative controls outlined
6 above, only the chartered banks are directly affected.
7 It would appear that if credit control is to be fully
8 effective, other bodies which accept deposits and make
9 loans (i.e. trust companies, finance companies, etc.)
10 should be subject to equally effective regulations.
11 (Report of the Governor of the Bank of Canada to the
12 Minister of Finance for 1956, pages 26-27, and also
13 - James Muir - Annual Meetings of The Royal Bank of
14 Canada on January 10, 1957 and January 14, 1960. See
15 Exhibit 31).

16 (v) Moral Suasion

17 45. In addition to the above quantitative
18 controls, there is the aspect of qualitative control,
19 or moral suasion (or "open-mouth" policy, as it is
20 sometimes called) which is perhaps the most difficult to
21 describe of the tools available to a central bank.
22 Involved is an endeavour to cause some group, which has
23 some control over the extension of some type of credit,
24 to modify its policy temporarily. Theoretically, there
25 can be no compulsion and the "suasion" has no legal
26 backing. It is the closest the Bank of Canada can come
27 to selectivity in its endeavours to vary the availability
28 of credit.

29 46. To be successful, it is obvious that the
30 Governor must be held in high esteem by those whose



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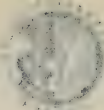


1 policy he seeks to influence. His prestige should not
2 be lessened by too frequent resort to moral suasion,
3 (since he is unlikely to be successful in every attempt)
4 his aims must be reasonable, and he must be able to
5 present his case with conviction to those concerned.
6 Threats or arbitrary action can not be used, since there
7 is no legal backing for either, and the request should
8 be for a temporary period only, otherwise, it might appear
9 that the Governor is disregarding the legislative powers
10 of parliament which would involve a change in regulation
11 supporter by law.

12 47. There is no way of knowing how often, nor
13 when, the three Governors of the Bank of Canada have
14 attempted to use moral suasion. However, some instances
15 have been referred to in the Governors' Annual Reports
16 and others have been commented upon in parliamentary
17 hearings. Some examples may be illuminating, since they
18 illustrate the scope of the attempts and their success,
19 or otherwise.

20 48. In 1936, the Bank influenced stock
21 exchanges and chartered banks to raise margin requirements
22 on loans against stocks. (Bank of Canada - Second Annual
23 Meeting of Shareholders, February 23, 1937, page 16,
24 and Standing Committee on Banking and Commerce, House of
25 Commons, June 27, 1944, see Exhibit 32).

26 49. In 1946, the chartered banks were requested
27 not to hold more than 90 per cent of their savings deposits
28 in government of Canada securities (ex bills) and to
29 limit the rate of earnings thereon. (Report of the
30 Governor of the Bank of Canada to the Minister of Finance



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1 for 1946, page 14. See Exhibit 33).

2 50. In 1948, it was suggested to the chartered
3 banks that it was undesirable to finance corporate
4 capital development through bank credit. (Report of the
5 Governor of the Bank of Canada to the Minister of Finance
6 for 1948, pages 7-8. See Exhibit 34).

7 51. In 1951, the banks agreed to attempt to
8 limit further expansion of bank credit. (Report of the
9 Governor of the Bank of Canada to the Minister of
10 Finance for 1951, page 9. See Exhibit 35). In the same
11 year, the Bank may have asked life insurance companies to
12 limit their purchases of new-issue securities to current
13 income.

14 52. In 1955, the chartered banks agreed, at
15 the Bank's request, to endeavour to maintain a specified
16 porportion of secondary reserves.

17 53. Also in 1955, the chartered banks again
18 agreed to limit term lending and to report to the Bank
19 unused commitments for such lending. (Report of the
20 Governor of the Bank of Canada to the Minister of Finance
21 for 1955, pages 17-18. See Exhibit 36).

22 54. In 1956, the stock exchanges were urged
23 to curtail credit extended on a margin basis. (Report
24 of the Governor of the Bank of Canada to the Minister
25 of Finance for 1956, pages 33-34. See Exhibit 37).

26 55. Also in 1956, the Bank attempted to get
27 agreement from finance companies and departmental
28 stores to prevent increases in the extension of credit.
29 (Report of the Governor of the Bank of Canada to the
30 Minister of Finance for 1956, pages 34-35. See Exhibit 38).



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56. In 1957, the chartered banks were urged to maintain their rate of N.H.A. mortgage investment and the notional idea of separating savings and commercial deposits was re-introduced. (Report of the Governor of the Bank of Canada to the Minister of Finance for 1957, page 28. See Exhibit 39. The segregation of savings and commercial deposits was mentioned by Mr. Coyne in his 1956 Report, pages 9, 27 and 29. See Exhibit 40).

57. In 1959, the chartered banks agreed to be most careful in their lending policies and to avoid an increase in loans, if possible. (Report of the Governor of the Bank of Canada to the Minister of Finance for 1959, page 37. See Exhibit 41).

58. In 1960, in his Annual Report and in public addresses, the Governor stressed the concept that high interest rates were necessary in Canada to attract savings. This idea may also have been in his mind when the Bank supported the Conversion Loan in 1958.

59. In August, 1961, the Governor suggested to certain firms (all members of the I.D.A.C.) that it would be undesirable for borrowers to resort to the American market. This directive was rescinded in March, 1962. (Honourable Donald M. Fleming, House of Commons, March 19, 1962. See Exhibit 42).

60. Apparently, many of these suasion efforts were effective, while others, by the admission of the Governor, were not. Several are of special interest. The 1955-1956 inauguration of secondary reserves, which was achieved over the objections of the chartered banks,



56. In 1957, the chartered banks were urged to maintain their rate of N.H.A. mortgage investment and the notional idea of separating savings and commercial deposits was re-introduced. (Report of the Governor of the Bank of Canada to the Minister of Finance for 1957, para 26. See Exhibit 37. The notional idea of separating savings and commercial deposits was mentioned by Mr. Coyne in his 1956 Report, pages 9, 27 and 29. See Exhibit 40).

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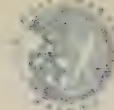
was achieved with the assistance of the chartered banks,



1 is still in effect. (One may wonder whether the
2 agreement should not be terminated). Another is the
3 specific reference by both Mr. Towers and Mr. Coyne to
4 chartered banks' savings deposits (as separated from
5 commercial deposits) where, the former limited holdings
6 of Canada bonds against them, and the latter sought to
7 have a proportion invested in mortgages. This leaves
8 open a possibility that, in order to influence liquidity
9 or the yield curve, attempts may be made some time to
10 have, for instance, chartered banks invest a minimum
11 amount of savings deposits in long-term Canada bonds.
12 There are, of course, many variations of this theme
13 which could be played for investing institutions. Aside
14 from the temporary alleviations which moral suasion, when
15 successful, may attain, it may in future be a proving
16 ground, indicating the desirability and practicability,
17 or otherwise, of legislative changes in the Acts
18 respecting the Bank of Canada, the chartered banks,
19 insurance companies, etc. The following matters, which
20 in the past have interested Governors of the Bank, should
21 perhaps be investigated thoroughly with such views in
22 mind.

23 i. Should the Bank of Canada have the
24 power to vary margin requirements
25 on loans for carrying stocks with
26 both chartered banks and stock
27 exchange member houses.

28 ii. Should the Bank of Canada have the
29 power to alter the terms (i.e. rates
30 of interest, down payments, periods



is still in effect. (One may wonder whether the agreement should not be terminated). Another in the specific reference by both Mr. Towers and Mr. Coyne to chartered banks' savings deposits (as separated from "other deposits") seems, the former stated, to be of interest to the public and the latter stated to have a proportion invested in mortgages. This leaves the question that, in order to influence the yield curve, attempts may be made some time to have, for instance, chartered banks invest a certain amount of savings deposits in long-term Canada bonds. There are, of course, many variations of this theme which could be played for investing institutions. Aside from the temporary alleviations which moral suasion, when successful, may attain, it may in future be a proving ground, indicating the desirability and practicability, or otherwise, of legislative changes in the Act respecting the Bank of Canada, the chartered banks, insurance companies, etc. The following statement in the past have interested Governors of the Bank, should perhaps be investigated thoroughly with such views in mind.

- i. Should the Bank of Canada have the power to vary margin requirements on loans for carrying stocks with both chartered banks and stock companies?
- ii. Should the Bank of Canada have the power to alter the terms (i.e. rates of interest, down payments, periods



of repayment) governing instalment purchases through finance companies, banks, etc.

iii. Should the Bank of Canada have direct power in regulating term lending (including N.H.A. mortgages) by banks. As opposed to public sale of securities, direct term lending by banks for capital expenditures involves the creation of deposits without any offsetting reduction in savings, and hence increases the money supply for as long as the loan is outstanding. This works against flexibility in monetary policy.

iv. Should the Bank of Canada have the power of establishing and varying the cash reserves of trust companies and other "near" banks.

VII. LIMITATIONS OF MONETARY POLICY

61. It is evident that, even when the aims of fiscal and monetary policy are harmonious, there are limitations to the extent of the efficiency of monetary policy in achieving its objectives. This has been recognized by the Macmillan Commission, as well as by the three Bank of Canada Governors, the Chairman of the Board of Governors of the Federal Reserve System, and the Governor of the Bank of England to name a few. (See Exhibit 43, for:



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the following report of the Macmillan Commission, 1926-27, p. 10.)



- 1 - Macmillan Report - paragraph 235.
- 2 - The Standing Committee on Banking and Commerce, Mr.
- 3 Towers Hearings, 1939 and March 23, 1954.
- 4 - Mr. Coyne, on whom the first protracted period of
- 5 restrictive policy fell, had the most to say. The
- 6 quoted comments are from his 1956 Report, pages 23-25,
- 7 and the 1957 Report, pages 17-18. His comments in
- 8 the 1959 and 1960 Reports are lengthy. See pages
- 9 3-10, and 16-23, respectively. His public speeches
- 10 in these years are also illuminating.
- 11 - Mr. Louis Rasminsky - comments made in a press release,
- 12 dated July 31, 1961, shortly after his appointment
- 13 as Governor of the Bank of Canada, and in his Report
- 14 to the Minister of Finance for 1961.
- 15 - Federal Reserve Bank of Philadelphia, "Quest for
- 16 Stability", pages 36 and 52.
- 17 - Remarks by Wm. McC. Martin before the Association of
- 18 Reserve City Bankers, April 11, 1961.
- 19 - Remarks by Lord Cobbold, Edinburgh, February, 1961.)
- 20 Fundamentally, it can only bring influence to bear in
- 21 a general way to create an atmosphere which may be
- 22 conducive to attaining the desired conditions. In
- 23 other words, it cannot be particular in the sense that it
- 24 can determine who will get a job and at what level of
- 25 pay, who can or will borrow money and at what rate,
- 26 what price an article will command, nor can it influence
- 27 price levels (nor supply and demand factors) in other
- 28 countries, which might lead to variations in exports and
- 29 imports for a country such as Canada.

30 62. It may be somewhat less evident, but a



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imports for a country such as Canada.

62. It may be somewhat less evident, but a



1 central bank may well have conflict from its own
2 functions in attaining its own objectives. In the case
3 of the Bank of Canada, this has been true. For example,
4 in periods when it has been attempting to stimulate the
5 economy by easing credit, it has had to sell bonds for
6 Government accounts such as the Unemployment Insurance
7 Fund. In periods of credit restraint, when the public
8 and the chartered banks have been sellers of government
9 bonds, (sometimes the public redeem their Savings Bonds,
10 and this could reach embarrassing proportions in times
11 of stress) it has had to support the market in order to
12 avoid chaotic conditions. It has also felt compelled to
13 stabilize the bond market before, during, and/or after,
14 government financing. Even in its capacity of lender
15 of last resort, it has had to extend credit temporarily,
16 when it wished to be restrictive. Furthermore, whether
17 ease or restraint is indicated, foreign exchange
18 stabilization or undesirable flows of foreign credit have
19 impinged on the effectiveness of desired policy and, of
20 course, mysterious changes in the velocity of circulation
21 have upset carefully calculated projections. However,
22 the Bank has, generally speaking, been ingenious in its
23 use of offsetting action and/or moral suasion under
24 these and other circumstances. Indeed, discounting the
25 probability which always exists for human error, it is
26 only in recent years when fiscal policy involving
27 continuing deficits and high taxation has taken
28 precedence over monetary policy, that Bank action has
29 become somewhat ineffective. Perhaps, the framers of
30 fiscal policy should examine the oft-quoted preamble to



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1 the Bank of Canada Act, and govern themselves accordingly.
2 In support of this last statement is the testimony of
3 Mr. Towers before the Standing Committee on Banking and
4 Commerce in 1939. (Memoranda and Tables re Bank of
5 Canada given before the Standing Committee on Banking and
6 Commerce, Chapter V, pages 47-50. Readers will find
7 that little updating is necessary. Mr. Coyne expressed
8 much the same thought in a speech entitled, "Sound Money
9 for Sound Growth" given on March 22, 1960. See Exhibit
10 44). The following excerpts are still applicable, even
11 though the hearings were held some 23 years ago: "My
12 first comment would be that most advocates of compensatory
13 deficit spending have developed their theory with tacit
14 reference to countries which to a far greater extent
15 than Canada, produce for internal consumption.

16 63. "Canadian thinking on this problem is
17 inevitably influenced by developments in theory and
18 practice which are taking place in the United States.
19 In that country only about one-twentieth of the national
20 income consists of receipts from goods and services sold
21 abroad. In Canada, the proportion is about one-third.
22 In the United States the problem of achieving full
23 employment and production is mainly one of offsetting or
24 compensating for a reduction in the private demand for
25 durable goods. No one would attempt to deny the
26 existence of a comparable problem in Canada; just because
27 our growth through the later twenties was so rapid the
28 drop in private demand for durable goods has been all the
29 more severe. But in Canada there is superimposed upon
30 this a problem which is perhaps more important and



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58. "Canadian thinking on this problem is inevitably influenced by developments in theory and practice which are taking place in the United States. In that country only about one-twentieth of the national income consists of receipts from goods and services sold abroad. In Canada, the proportion is about one-third. In the United States the problem of achieving full employment and production is mainly one of offsetting or compensating for a reduction in the private demand for durable goods. No one would attempt to deny the existence of a comparable problem in Canada; but because our growth through the latter twenties was so rapid the drop in private demand for durable goods has been all the more severe. But in Canada there is superimposed upon this a problem which is perhaps more important and



1 certainly more difficult, viz., what to do about a
2 reduction in the demand for goods and services which we
3 sell abroad.

4 64. "Deficit spending in Canada can have little
5 direct influence upon the course of foreign demand for
6 our products. It can do little to increase domestic
7 consumption of things which we normally export. Again,
8 because of the specialized character of the production
9 for which Canada is suited and equipped, it is unusually
10 difficult to meet a decline in foreign demand by creating
11 domestic demand for new things which this country can
12 produce at a reasonable cost. And the necessary shifts
13 of man-power and equipment might be definitely wasteful
14 if the fall in export demand turned out to have been only
15 of short duration.

16 65. "There are, therefore, greater limitations
17 upon what compensatory deficit spending can do to offset
18 fluctuations in the Canadian economy than there would
19 be in the case of a more diversified and self-sustaining
20 country. There are also greater dangers involved, as I
21 shall now indicate.

22 66. "An export economy is in the position of
23 having very little influence over the level at which many
24 of its most important prices are set. It should, there-
25 fore, do all it reasonably can to keep its costs flexible
26 and to avoid introducing elements of rigidity through
27 borrowings on fixed terms. Otherwise its competitive
28 position in foreign markets may be adversely affected.

29 67. "I have already indicated why I think
30 compensatory spending is likely to have less influence



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1 upon the course of real national income in this country
2 than it would in most others. When large government
3 expenditures are being made and debts are mounting
4 rapidly, there will presumably be relatively less to show
5 for them in the way of an immediate expansion of
6 activity, and the possibility of harmful reactions upon
7 private confidence and spending will be relatively
8 greater."

9 68. "The apprehension which large government
10 deficits may arouse in the minds of business men and
11 investors, even if it happens to be initially ill-founded,
12 is none the less real. If it is sufficiently strong it
13 tends to bring about its own realization, and is
14 accordingly a factor which warrants most careful
15 consideration when deciding upon fiscal policy.

16 69. "Another of the main arguments advanced by
17 opponents of a compensatory deficit policy is that it may
18 lead to inflation. In the case of a largely self-
19 contained economy general inflation is unlikely to
20 occur so long as appreciable reserves of productive
21 capacity remain in idleness. In the case of Canada,
22 however, one must also take account of the fact that,
23 under present conditions, there are fairly definite
24 limitations upon the range over which domestic
25 production can compete with imports on a cost basis. At
26 least part of the active spending power created by
27 government deficits is likely to increase imports
28 rather than give work to unemployed Canadian men or
29 machines. If the increase in imports is not offset by
30 increased exports (or by borrowing abroad) the external



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1 value of the Canadian dollar will tend to fall and
2 Canadian prices will tend to rise. In other words, the
3 mere existence in Canada of large amounts of unused
4 capacity does not in itself preclude an inflationary rise
5 in prices."

6 70. Mr. Towers, in one of his rare public
7 addresses recently stated: (Address, on January 25th,
8 1962, to the Annual Meeting of The Canada Life Assurance
9 Company, in his capacity as Chairman of the Board)

10 ".....The fact that per capita Gross National Product is
11 less in real terms than it was five years ago, combined
12 with unemployment that has persisted at too high a level,
13 should inspire a most serious and objective search for
14 the reasons behind this unsatisfactory situation.....

15 71. "In searching for reasons to explain
16 Canada's unsatisfactory economic performance during the
17 last five years, I have mentioned the international over-
18 supply situation confronting many of our major extractive
19 industries and the possibility that the overall burden of
20 taxation and an over-valued currency have had a depressing
21 effect on our affairs. All these things have a bearing
22 on our costs and prices. There is the further
23 possibility -- indeed probability -- that other factors
24 have been operating to push our costs out of line with
25 the rest of the world's. Wage rates are not the only
26 factor in costs of production but they are a very
27 important one, and, if increases in rates are in excess
28 of increases in the productivity of labour, the end
29 result is unemployment, balance of payments difficulties
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1 72. ".....international conditions have been
2 changing rapidly since 1956 and we have to compete with
3 a number of major countries which, so far at least,
4 appear to have had relative success in keeping their
5 costs of production in line. When this situation gives
6 rise to unused capacity and unemployment in the higher
7 cost countries, attempts to stimulate the economy by
8 public spending and monetary expansion can hardly be
9 regarded as effective long-term solutions."

10 73. Confirming Mr. Towers' thoughts (but
11 referring to the United States) is the following extract
12 from the highly respected monthly letter of the First
13 National City Bank for November, 1961. ".....there is
14 a "mysterious tag" on government dollars. It says right
15 on our coins and paper money that they are issued by the
16 authority of government. Government spending can be
17 financed by monetary inflation, by use of sovereign powers
18 of money issue. Private spending, under the discipline
19 of income flow and creditworthiness, lacks power to
20 create inflation of truly "explosive" dimensions.
21 Government has unique power to increase spending, and
22 not only through money issue but also through taxation
23It may be observed that an increasing proportion
24 of federal expenditures is in welfare categories where
25 there are no goods produced or services provided as a
26 counterpart for the income given. These payments,
27 however great their social merits, subtract from needs
28 to work, from production, and from flows of goods
29 and services in the markets.....Then there is the
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1 the demand of government for more money to spend.
2 Concentrated on working people as a class, they subtract
3 from human effort and from the ability of the private
4 business system -- which puts the goods on the shelves
5 of the stores -- to finance innovations which lower
6 production costs and prices.....Although there is a
7 view that rising curves of government spending can
8 stimulate economic growth, the evidence points to the
9 contrary conclusion: over-rapid growth of government
10 spending and taxing obstructs balanced growth of the
11 whole economy. The only time in the past decade that
12 business fixed investment moved up to a higher plateau
13 was in 1956-57, after the 1954 cutbacks in government
14 spending and taxes.....Thus, through the tax system
15 used to raise them, government dollars obstruct
16 progress and hence the flows of goods in the market that
17 give real value to money."

18 74. Observers of the Canadian economic scene
19 will be well aware that text books and tradition throw
20 little light on the problem of continuing budgetary and
21 cash deficits which have become the pattern here,
22 regardless of contraction or expansion in the nation's
23 economy, and despite stifling levels of taxation.
24 Government embarked on an enlarged spending program and
25 broader welfare payments a few years ago, presumably to
26 alleviate unemployment problems. Evidence of success
27 from this policy is inconclusive. In the meantime,
28 the atmosphere which has been created is one of
29 apprehension and concern, hardly the basis for broad
30 economic development. It is urgent that the present

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Concentrated on working people as a class, they subtract the demand of government for more money to spend.



government (and those to follow) return to fiscal orthodoxy and take steps to move toward cyclically balanced budgets, thus bringing fiscal and monetary policies together harmoniously.

VIII. RECOMMENDATIONS AND SUGGESTIONS

Reference

75. In the above text, recommendations have been made and suggestions advanced which involve further discussion before arriving at definite conclusions. Perhaps, the most important matter discussed is the Canadian Government's fiscal policy which has involved continuing deficits and stifling rates of taxation, but does not appear to have been particularly effective in stimulating the economy to the point where full use can be made of excess plant capacity and labour supply. Such a policy tends to create import demand, put strains on exchange rates, and creates distrust of the intrinsic value of the currency both internally and internationally and may lead, ultimately, to disruption of savings and investment programs. It has made monetary policy and the central bank quite ineffective. It is of prime importance that a more appropriate fiscal policy be developed in Canada.

para.
62-74
Exhibit
44

76. Other recommendations are summarized in the following paragraphs. They appear, more or less, in the order in which they have been



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VI. CONCLUSIONS AND RECOMMENDATIONS

Introduction

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Balance of Payments

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Exhibit
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the following paragraphs. They appear, more

or less, in the order in which they have been



discussed in the text above, and no attempt has been made to present them in order of importance.

77. Amendments should be made to the Bank of Canada Act clarifying the Bank's relationship with the Government. Procedure to be followed in the event of the resignation of the Governor, either by his own volition or by request, should be established.

78. In order to eliminate a serious conflict of interest position, debt management should revert to the Department of Finance, from the Bank of Canada. The Department should regularly make use of advisory committees from the dealers and banks. The number of primary distributors used in government financing should be reduced, and include only those who ~~usually~~ position government securities and who regularly make markets.

79. In an endeavour to restore confidence in and broaden the mid and long-term segments of the government market, consideration might be given as to whether selected dealers should obtain "lender of last resort" facilities, from the Bank of Canada, against collateral of government bonds maturing in more than three years with special flexible call loan facilities at chartered banks. Less emphasis should be placed on Canada Savings Bonds as a means of saving, rather than a medium for



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Para. 7

Exhibit

Para. 8-13

5-7

para. 16



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80. The Bank of Canada's research department

Para. should make available informative pamphlets,
17

Exhibit which would clarify the Bank's functions,
11 actions and intentions, to complement available
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81. The Bank of Canada's Board of Directors

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12 to be selected from dealers and banks.

82. The Bank of Canada's open-market

operations should be confined to securities in

Para. the money market range of three years and
21-28 &
35

Exhibits under and, when possible, emphasis should be
13-19 on operations in the bill market. The only
16 exception should be in the event of a disorderly
17 market situation, or when operations are for
18 some Government account.

83. The Bank of Canada's trading departments in

Toronto and Montreal should be enlarged and

Para. traders given more authority, in order to
29-30

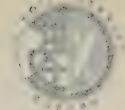
Exhibit facilitate trading and to enable the Bank to
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24 Bank's trading should be limited to those
25 organizations which regularly make markets in
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the Government's exchange policy. Among other

things, Canada's position vis-a-vis The

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1 decisions should be reached concerning the
2 Para. adequacy, or otherwise, of our exchange
3 36-37 reserves and holdings of gold, and conclusions
4 Exhibits should be made as to the desirability, or
5 22-23 otherwise, of the Canadian dollar being
6 "pegged" in relation to other currencies.
7 85. The Bank of Canada's discount rate should
8 cease to "float" $\frac{1}{4}$ per cent above weekly
9 Para. treasury bill awards, and become administered.
10 41-43 Changes in rate, when deemed necessary, should
11 Exhibits be accompanied by an explanatory statement by
12 28-30 the Governor of the Bank, and on occasion,
13 supported by a statement from the Minister of
14 Finance.
15 86. Other matters have been mentioned, but
16 further examination and discussion seems to be
17 indicated before recommendations can be made.
18 These suggestions are outlined in the following
19 paragraphs.
20 87. The Commission might consider whether, if
21 Para. the Department of Finance assumes the debt
22 13 management function, it would be desirable for
23 Exhibit dealer syndicates to underwrite direct and/or
24 7 guaranteed (e.g. CNR) financing.
25 88. The Commission might examine whether
26 Para. chartered bank secondary reserves, which were
27 40 & 60 instituted through moral suasion in 1956,
28 Exhibits should continue to remain in effect.
29 26-27
30 89. The use of "moral suasion" by the Bank
of Canada has been quite extensive, and



decisions should be reached concerning the adequacy, or otherwise, of our exchange reserves and holdings of gold, and conclusions should be made as to the desirability, or otherwise, of the Canadian dollar being "pegged" in relation to other currencies.

85. The Bank of Canada's discount rate should cease to "float" $\frac{1}{4}$ per cent above weekly changes in rate, when deemed necessary, should be accompanied by an explanatory statement by the Governor of the Bank, and on occasion, supported by a statement from the Minister of Finance.

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Exhibits
28-29

Exhibits
28-30

Exhibits
40 & 60

Exhibits
26-27



information gained in its application might
Para. be examined to see whether the Bank of Canada
44-60
should have additional powers to influence
Exhibits
31-42 such items as stock margins, terms relative to
instalment sales, term lending by chartered
banks, and reserves for "near" banks.

EXHIBITS

Exhibit 1. Macmillan Report

219. The functions discharged by a central bank
being of such vital importance to the economic and
financial life of a country, it is perhaps natural to
ask whether they could not be adequately performed by
some direct organ of government. It has in practice
been found that a central bank can give most effective
service to the community if it is free from the feat of
interference for political ends in operating the delicate
mechanism of the national monetary and financial machine
.....it has been found that there are preeminent
advantages to the state in entrusting the special and
highly technical functions of a central bank to a body
not subject to the vicissitudes of political life.

Exhibit 2. Macmillan Report

206.the central bank,....., should
endeavour to regulate credit and currency in the best
interests of the economic life of the nation and should
so far as possible control and defend the external value
of the national monetary unit.....from the inter-
national point of view, the central bank by wise and
timely co-operation with similar institutions in other



1 countries, should seek, so far as may lie within the
2 scope of monetary action, to mitigate by its influence
3 fluctuations in the general level of economic activity.
4 These functions do not, of course, exhaust the tasks
5 of a central bank. Within a state, the central bank
6 should, in addition, be a ready source of skilled and
7 impartial financial advice at the disposal of the
8 administration of the day.....

9 207. It is easily possible to expect either
10 too much or too little of central bank action. A central
11 bank is at the same time an instrument and a force.
12 As an instrument it is the means by which the state -
13 which must necessarily retain ultimate sovereignty in
14 matters affecting the currency - can give effect to the
15 national policy. As a force the central bank has certain
16 powers in its keeping which can be used to achieve the
17 ends of national policy. Clearly these powers are of
18 differing efficacy according to the aim of the policy.
19 A central bank cannot be expected to influence the price
20 of a particular commodity. It is even not desirable
21 that a central bank should be specifically charged with
22 any responsibility for the general price level of a
23 country. There are many factors, of varying nature,
24 which combine to influence that level and a central bank,
25 working as it does purely in the monetary sphere, cannot
26 be expected to have complete control, though it may well
27 have a measure of influence. If it attempted to
28 exercise any drastic control it would have to wield powers
29 far beyond those which any body other than the sovereign
30 authority would be entitled to exercise. It is manifest,



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too much or too little of central bank action. A central
bank is at the same time an instrument and a force.
As an instrument it is the means by which the state -
which must necessarily retain ultimate sovereignty in
matters affecting the currency - can give effect to the
national policy. As a force the central bank has certain
powers in its keeping which can be used to achieve the
ends of national policy. Clearly these powers are of
differing efficacy according to the aim of the policy.
A central bank cannot be expected to influence the price
of a particular commodity, or to even to maintain
that a central bank should be specifically charged with
any responsibility for the general price level of a
country. There are many factors, of varying nature,
which combine to influence that level and a central bank,
working as it does purely in the monetary sphere, cannot
be expected to have complete control, though it may well
exercise any drastic control it would have to wield powers
far beyond those which any body other than the sovereign
authority would be entitled to exercise. It is manifest,



1 however, that the regulation of the volume of credit is
2 an important factor, in influencing the level of economic
3 activity and therefore of prices and this is one of the
4 cardinal tasks of a central bank.....The regulation of
5 the quantity of credit is effected by the action of the
6 central bank on the reserves of the commercial banks.
7 By increasing or diminishing these reserves, or by
8 increasing the cost of securing them, there is set in
9 motion a process of expansion or contraction through the
10 ordinary channels of banking.....

11 208. In the control over the external value of
12 the monetary unit the action of the central bank is
13 also of major importance. This function, indeed, is a
14 logical outcome of that of credit regulation. Whatever
15 additional influences may affect the level of the
16 exchanges, such as short term capital movements, external
17 borrowings and indebtedness, and the income from overseas
18 investments, the long term factor of decisive importance
19 is the credit structure of the country, and no modern
20 state can afford to dispense with the most effective
21 controlling instruments.

22 209. The services which a central bank may
23 perform in the international sphere are even less easily
24 dispensed with in the modern world than those which it
25 can render within the borders of a state. Whatever changes
26 may occur in the volume of international trade and the
27 comparative positions of various countries, there has
28 never been a time when external financial inter-relation-
29 ships have assumed more importance than in the last
30 decade.....



...that the regulation of the money market is an important factor, in influencing the level of economic activity and therefore of prices and this is one of the cardinal tasks of a central bank.....The regulation of the quantity of credit is effected by the action of the central bank on the reserves of the commercial banks. By increasing or diminishing these reserves, or by increasing the cost of securing them, there is set in motion a process of expansion or contraction through the ordinary channels of banking.....

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210. The precise degree to which the level of economic activity in the world as a whole may be influenced by concerted international monetary action, may be a matter of opinion, but that a common direction in monetary policy may have an important influence in avoiding economic excesses or in stimulating revival is beyond dispute. The co-operation of central banks is beset with many difficulties; its effects are limited or distorted by many non-monetary influences; but if we wish to continue that mutual interchange of goods and services which in the past has stimulated the economic life of all parts of the world, we ought to use all possible means of bringing order into the realm of international relations. In the monetary sphere the germ of such order is to be found in the inter-relations of central banks working to harmonize national policy with the needs of the international situation.

218. To enable it to discharge the essential functions to which we have referred above, modern experience tends to show that certain definite principles should be observed in the constitution of a central bank. Thus, in order that it may regulate credit and currency, it is essential that the central bank should hold a suitable proportion of the cash reserves of the commercial banks. It is essential for the full and satisfactory working of a central bank, that it should have the sole right of issue of legal tender notes; it is essential that the central bank, as the financial adviser of the Government, should in due course hold the various Government accounts and carry out, on behalf of the Government all financial transactions.

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229.It may indeed be the case that in the absence of a highly developed money market the control of a central bank in Canada over the financial system could not be as sensitive as that which is exercised, for instance, by the Bank of England in the United Kingdom. The fact, however, that a new institution in Canada would not be able to employ all the instruments of control exercised in an older and financially more highly developed country, seems to us an inadequate reason for omitting to develop such control as could undoubtedly be achieved. The financial system and economic life of Canada are already sufficiently well developed to make the instruments of the discount rate, the purchase and sale of securities, and operations in the foreign exchange market, of sufficient importance in the hands of a well-managed central bank to give it a decisive influence on the credit situation in Canada.

230. Canada is a country with a relatively large volume of external trade and a heavy external indebtedness and is, therefore, especially interested in the international value of her currency. The holding of gold and foreign exchange by the central bank should and could become a factor of the first importance in carrying out the national policy in regard to the external value of the currency. It is no part of the functions of a central bank to monopolize the exchange markets. Here, as in the case of credit control, its function is to impart or counteract a trend as circumstances require, and this task, even from an early date, would be within the capacity of a Canadian central bank.



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1 Exhibit 3. G.F. Towers' 1st Report

2 The functions of a central bank are well set
3 forth in the report of the Royal Commission on Banking and
4 Currency in Canada. The chief functions are to endeavour
5 to regulate the volume of credit; to defend the external
6 value of the national monetary unit; to be a ready source
7 of skilled and impartial advice at the disposal of the
8 Government (in the case of Canada, the Dominion and
9 Provincial Governments); and to afford timely co-operat-
10 ions with the central banks of other countries.....

11 Exhibit 4. Hon. J.L. Ilesley-- House of Commons 1941.

12The Bank of Canada was created by
13 parliament as an autonomous corporation with its stock
14 owned wholly by the government, but with its own
15 management and board of directors appointed by the
16 government. It is an arm of the government, but not a
17 department of the government. The character of the act
18 is such that responsibility for its operations is placed
19 squarely on the shoulders of the governor and the board
20 of directors..... The point which I would like to
21 emphasize is that the responsibility with which the gov-
22 ernor and board have been charged by parliament does not
23 in any way relieve the government of the responsibility
24 for the monetary policy being pursued by the Bank, nor
25 in any way militate against public control of monetary
26 policy. The monetary policy which the bank carries out
27 from time to time must be the government's monetary policy,
28 but the government must leave the carrying out of that
29 policy, the choice of ways and means of executing it,
30 to the management of the bank in whose judgment it has



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Finance in Canada. The chief function was to regulate

to regulate the volume of credit; to defend the external

value of the national monetary unit; to be a source of

an elastic and immediate source of the disposal of the

Government (in the case of Canada, the Dominion and

provincial governments) and to act as a clearing house

for the central banks of other countries.....

Exhibit 4. Hon. J.L. Flaherty--House of Commons 1911.

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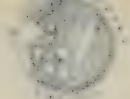
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1 confidence. If the government is satisfied with the
2 policy which is being pursued, there is obviously no
3 quarrel between it and the bank. Let us suppose, however,
4 that the management of the bank and the government do not
5 see eye to eye in the matter of monetary policy.....In
6 such a case there can be no question whatever as to the
7 outcome of the dispute. The government's view will
8 prevail. In view of the statutory responsibility
9 placed on the governor and the board of directors, I do
10 not believe that those of them who disagreed with the
11 government on a fundamental issue could conscientiously
12 carry out the government's policy. It would therefore be
13 necessary for them to resign, and they would be replaced
14 by others who were willing to accept responsibility for
15 the type of policy which the government believed to be
16 appropriate.

17 G.F. Towers -- House of Commons, 1954.

18The situation is that parliament has
19 placed squarely on the shoulders of the directors and
20 management of the Bank of Canada the responsibility for
21 monetary policy. It would be of no use for us to come
22 before a committee of this kind and say in respect of
23 certain actions which were criticized, we did not like
24 that but the government wanted us to do it.....We must
25 and do take full responsibility for everything which we
26 have done.....There is no alibi possible for the central
27 bank. On the other hand, there is no alibi possible
28 for the government, because if government said: well, we
29 disagreed with what the central bank did, but parliament
30 has placed the responsibility on them, so what could we



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bank. On the other hand, there is no alibi possible
for the government, because it is responsible for the
direction with which the central bank and the government
has placed the responsibility on them, so what could we



1 do? The answer obviously is that the administration of
2 the day, supported by a majority in parliament, can always
3 alter the legislation. In fact, I doubt whether a
4 disagreement would ever necessitate such a thing, because
5 there are various ways and means by which directors and
6 management can be got rid of.....There is a long history
7 behind this thing in central banking.....Just to make
8 sure that nothing I have said conveys a misunderstanding,
9 I would like to add that no central bank, and certainly
10 not the Bank of Canada has any delusions of grandeur or
11 any thought that it has sovereign power that always lies
12 with the administration which commands a majority in
13 Parliament.

14 J.E. Coyne - House of Commons, 1956.

15if the government of the day were suff-
16 iciently displeased with the bank or the management of
17 the bank, they could put in motion steps which would bring
18 about a change in the management. At some stage in that
19 process, if the government were so determined as to make
20 a real issue of it, a public issue presumably, the
21 governor would have to resign.....I do not think it follows
22 from that -- I am sure Mr. Towers did not mean it to
23 follow from that, -- that because the government can
24 bring about the removal of the governor of the bank,
25 therefore, the governor of the bank must do whatever the
26 government wants him to do. Nor does it follow in fact
27 that the government expresses views of a kind that
28 would require action by the bank contrary to its own
29 views of what should be the appropriate monetary policy
30 at that time. Certainly parliament is supreme, and the



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J.R. Coyne - House of Commons, 1966.

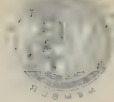
.....If the government of the day were suddenly displaced with the bank on the management of the bank, they could not do anything which would result about a change in the management. At some stage in that process, if the government were so determined as to make a real issue of it, a public issue presumably, the Governor would have to resign.....I do not think it follows from that -- I am sure Mr. Towers did not mean it to follow from that, -- that because the government can bring about the removal of the Governor of the bank, therefore, the Governor of the bank must do whatever the government wants him to do. Nor does it follow in fact that the government expresses views of a kind that would require action by the bank contrary to its own view in that matter on the basis of its statutory powers at that time. Certainly Parliament is supreme, and the



1 government, having a majority in parliament, is in a
2 position, if it thinks strongly enough about a matter,
3 to bring about a change in the management of the bank.....

4 Louis Rasminsky - July 31, 1961 Statement.

5 I believe that it is essential that the
6 responsibilities in relation to monetary policy should
7 be clarified in the public mind and in the legislation.
8 I do not suggest a precise formula but have in mind two
9 main principles to be established; (1) in the ordinary
10 course of events, the Bank has the responsibility for
11 monetary policy, and (2) if the Government disapproves
12 of the monetary policy being carried out by the Bank it
13 has the right and the responsibility to direct the Bank
14 as to the policy which the Bank is to carry out. The
15 first principle is designed to ensure that the Bank has
16 the degree of independence and responsibility necessary
17 if it is, in the language of the Bank of Canada Act, "to
18 regulate credit and currency in the best interests of
19 the economic life of the nation". To discharge this
20 duty the Bank must be sufficiently independent and
21 responsible in its operations to be able to withstand
22 day-to-day pressures from any source. But in the longer
23 run, if there should develop a serious and persistent
24 conflict between the views of the central bank with
25 regard to monetary policy which, after prolonged and
26 conscientious efforts on both sides, cannot be resolved,
27 the Government should be able formally to instruct the
28 Bank what monetary policy it wishes carried out and the
29 Bank should have the duty to comply with these instructions.
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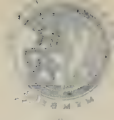
1 place on Government direct responsibility for the
2 monetary policy to be followed. If this policy, as
3 communicated to the Bank, was one which the Governor felt
4 he could not in good conscience carry out, his duty would
5 be to resign and to make way for someone who took a
6 different view.

7 Exhibit 5. G.F. Towers 1938 Report

8 Acting under powers conferred by section 23(2)
9 of the Bank of Canada Act, you required the Bank, as
10 from April 1st, 1938, to act as Agent for the Government
11 in the payment of interest and principal and generally
12 in respect to the management of the public debt of
13 Canada. The Public Debt Division of the Bank was
14 constituted for this purpose and on April 1st last the
15 staff of the Loans and Interest Branch of the Department
16 of Finance entered our service. In view of the fact
17 that so much of the work of the former Loans and Interest
18 Branch had been interwoven with work performed by the
19 Bank in its capacity as fiscal agent of the Dominion
20 Government, we believe that the amalgamation will be in
21 the interest of efficiency and economical operation.

22 Exhibit 6. R.V. Roosa - Federal Reserve Operations

23 Most of the bidders for small amounts, and many
24 others up to the limit of \$200,000 per subscriber, submit
25 noncompetitive tenders which are allotted in full at the
26 average price determined by the accepted competitive
27 tenders (about one sixth to one eighth of the total bill
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1 Exhibit 7.

2 For many years, government-guaranteed C.N.R.
3 financing was handled in this way. When it was taken over
4 by the Bank of Canada in 1951, Mr. Donald Gordon, the
5 Railway's President and formerly a deputy governor of the
6 Bank, expressed his regrets to the Syndicate managers
7 and commended them for their efforts in the past. It may
8 be completely without significance, but in the past three
9 or four years, C.N.R. financing has caused not a little
10 disturbance in the bond market. Mr. J.E. Coyne in a
11 speech entitled, "Credit and Capital" made on December
12 14, 1959, stated, in part: ".....What is perhaps not so
13 widely recognized is that we also have in Canada a well
14 developed nation-wide capital market, particularly in
15 respect of the distribution of securities issued by
16 governments, local authorities and business corporations.
17 This is primarily the field of activity of investment
18 dealers. I think there is little doubt that the
19 financial machinery existing in Canada for the placing of
20 new issues of securities on the market is the equal of
21 that of any country in the world and, in proportion to
22 our size, it probably arranges, year in and year out,
23 for the provision of a greater quantity of new capital
24 to those requiring it than is the case in any other
25 country in the world. The results achieved are a
26 reflection of the industry and enterprise and broad
27 national outlook of our investment dealers,....."

28 Exhibit 8. G.F. Towers - 1953 Report.

29 A broad and active demand for short-term
30 government securities is an essential feature of an

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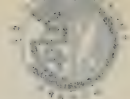


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2 Canada has always endeavoured to encourage the growth of
3 a short-term market in this country and several further
4 steps in this direction were taken during 1953. The
5 Government of Canada changed its regular offers of
6 treasury bills from a fortnightly to a weekly basis and
7 made available 273-day bills in addition to the usual
8 91-day bills, both of which developments found favour
9 with the market and increased the demand for and turnover
10 in such securities. In the year just past the Bank of
11 Canada instituted purchase and resale agreements with
12 bond dealers who take a jobbing position in the short-
13 term Government of Canada market. Under these arrange-
14 ments a dealer may within agreed limits sell treasury
15 bills and short-term Government of Canada bonds to the
16 Bank of Canada with an undertaking to repurchase them
17 over a short period at a predetermined yield to the Bank.

18 These arrangements offer jobbers an alternative
19 method of financing inventories of such securities so
20 that they are at all times able to meet the requirements
21 of their customers, including other bond dealers who
22 only occasionally have transactions in short term
23 securities.....

24 Exhibit 9. G.F. Towers - House of Commons, 1954.

25 The term "money market" is widely used but
26 seldom defined and indeed it is not easy to give it a
27 precise definition. The particular sector of the overall
28 financial market which it describes has varied from
29 country to country and from time to time. I think a
30 general definition would include any markets for financial



effectively functioning money market. The Bank of Canada has always endeavoured to encourage the growth of a short-term market in this country and several further steps in this direction were taken during 1953. The Government of Canada changed its regular offers of treasury bills from a fortnightly to a weekly basis and made available 273-day bills in addition to the usual 91-day bills, both of which developments found favour with the market and increased the demand for and turnover in such securities. In the year just past the Bank of Canada instituted purchase and resale agreements with bond dealers who take a jobbing position in the short-term Government of Canada market. Under these arrangements a dealer may within agreed limits sell treasury bills and short-term Government of Canada bonds to the Bank of Canada with an undertaking to repurchase them over a short period at a predetermined yield to the Bank. These arrangements offer jobbers an alternative method of financing inventories of such securities so that they are at all times able to meet the requirements of their customers, including other bond dealers who only occasionally have transactions in short term securities.

Exhibit 9. G.F. Towers - House of Commons, 1954.

The term "money market" is widely used but seldom defined and indeed it is not easy to give it a precise definition. The particular sector of the overall financial market which it describes has varied from country to country and from time to time. I think a general definition which would cover the financial



1 assets in which individuals, corporations and financial
2 institutions invest their short-term funds, and in which
3 a certain amount of turnover, or buying and selling, goes
4 on fairly continuously. It is a market for the
5 temporary employment of cash balances.

6 In Canada, Treasury Bills and other Government
7 of Canada short-term securities are by far the most
8 important categories of assets involved at the present
9 time. Commercial bills and similar instruments which are
10 an important factor in the money market in London, for
11 example, have played and are likely to play a negligible
12 role in Canada. In this country they are held
13 exclusively by banks and there is no trading even
14 between banks in this type of paper. There are a number
15 of other types of securities or assets which may be said
16 to be actually or potentially on the fringes of the money
17 market. For example, the larger provincial governments
18 have a substantial volume of short-term debt outstanding,
19 some of it bearing the name of Treasury Bills. At present
20 there is no trading in these Bills and they are in reality
21 just another form of short-term loan to a province by its
22 banker or bankers. They might, however, develop
23 sufficient tradeability in future to be classed as money
24 market paper. Again, while there is no call loan market
25 in Canada dealing in loans which can be called on really
26 short notice and which are made on an impersonal basis,
27 the type of bank loan which stockbrokers and investment
28 dealers presently use to finance their inventories might
29 in future develop in the direction of being a true money
30 market type of asset.

assets in which individuals, corporations and financial institutions invest their short-term funds, and in which a certain amount of turnover, or buying and selling, goes on fairly continuously. It is a market for the

In Canada, Treasury Bills and other Government of Canada short-term securities are by far the most important categories of assets involved at the present time. Commercial bills and similar instruments which are an important factor in the money market in London, for example, have played and are likely to play a negligible role in Canada. In this country they are held exclusively by banks and there is no trading even between banks in this type of paper. There are a number of other types of securities or assets which may be said to be actually or potentially on the fringes of the money market. For example, the larger provincial governments have a substantial volume of short-term debt outstanding, some of it bearing the name of Treasury Bills. At present there is no trading in these Bills and they are in reality just another form of short-term loan to a province by the banker or bankers. They might, however, develop sufficient tradability in future to be classed as money market paper. Again, while there is no call loan market in Canada dealing in loans which can be called on really short notice and which are made on an impersonal basis, the type of bank loan which stockbrokers and investment dealers presently use to finance their inventories might in future develop in the direction of being a true money market type of asset.



1 I would not include in my definition of the
2 money market such specialized markets as the stock
3 exchanges and the foreign exchange market owing to the
4 fact that it is not their primary function to provide a
5 liquid form of asset for the investment of short-term
6 balances. For practical purposes then, the Canadian
7 money market consists at the present time of all the
8 buyers and sellers of Treasury Bills and other short-term
9 Government of Canada securities. This will always be
10 the core of the Canadian money market, and only as breadth
11 and volume is developed in this area is it likely that
12 the boundaries of the money market can be extended as
13 widely as in larger and older financial communities.

14 Now I would like to say a few words about the
15 functions of the money market. In general, I believe
16 that one can say that its function is basically the same
17 as that of any market in a competitive economy whether
18 it deals in financial or physical assets. A good market,
19 by promoting wide competition between sellers and
20 providing wide choices to users, tends to distribute
21 resources where they are used with maximum efficiency.
22 Short-term capital, like any other commodity or service,
23 is likely to be forthcoming in optimum amounts and to be
24 most efficiently used if it is subject to the incentives
25 and disciplines which are provided by a broad market.
26 In Canada, where I think we can look forward to rapid
27 growth and a correspondingly large demand for capital,
28 and where there is considerable scope for Canadian
29 capital to displace external sources of financing, we
30 clearly need to use our own sources of short-term as well



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1 as long-term capital as effectively as possible.
2 Moreover, the kind of financial machinery needed to
3 provide a good short-term Government securities market
4 will also help to provide better facilities for long-
5 term financing.

6 Exhibit 10. J.E. Coyne - 1954 Report

7 The introduction in mid-June of what are known
8 as day-to-day loans was an important development affect-
9 ing both banking practices and the short-term securities
10 market or "money market". These loans are made by
11 chartered banks against the pledge of treasury bills
12 and Government of Canada bonds maturing within three
13 years. The borrowers are those bond dealers who are
14 prepared to act as jobbers in the short-term market and
15 who have entered into purchase and resale arrangements
16 with the Bank of Canada. Day-to-day loans may be called
17 for payment at any time and the willingness of the Bank
18 of Canada to purchase securities under resale agreements
19 provides an underlying assurance of liquidity.

20 From January 1953 to June 1954 the Bank of
21 Canada had made a considerable amount of funds available
22 for the financing of dealers' inventories of treasury
23 bills and short-term Government bonds through purchase
24 and resale agreements. The total provided in this way
25 reached a maximum of \$73 million in June. Subsequently,
26 day-to-day loans from the chartered banks provided this
27 financing in amounts which, as at the close of business
28 on Wednesdays, varied between a low of \$44 million and
29 a high of \$135 million, and Bank of Canada facilities
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1 In addition to providing a source of funds to
2 finance dealers' inventories of short-term Government
3 securities, day-to-day loans afford a convenient and
4 efficient means whereby the chartered banks may adjust
5 surplus or inadequate cash reserve positions. A bank
6 desiring to replenish its cash reserves may call part
7 or all of its day-to-day loans and present the borrower's
8 cheque through the Clearing House for credit to its
9 account with the Bank of Canada the following day. (A
10 bank can obtain additional cash on the same day by
11 borrowing from the Bank of Canada. In the case of sales
12 of treasury bills, Government of Canada bonds maturing
13 within 5 years, and longer-term Government of Canada
14 bonds, market practices respecting delivery and payment
15 dates have the result that cash is received on the
16 second, third and fourth days, respectively, after the
17 day of the sale.) When the day-to-day loan rate is
18 below the Bank Rate, as has consistently been the case,
19 the borrower whose loan is called has a strong incentive
20 to obtain the funds required to repay the loan from
21 another chartered bank which has surplus cash, rather
22 than from the Bank of Canada under a purchase and resale
23 agreement. One of the effects of the call and the new
24 loan is to transfer deposits at the Bank of Canada from
25 the lending to the calling bank. If the borrower is
26 not successful in obtaining a day-to-day loan from
27 another bank and obtains the funds from the Bank of
28 Canada, the initial effect is to increase the total
29 cash reserves available in the system, as the calling
30 bank receives an addition to its cash without a



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1 corresponding decrease in any other bank's cash.

2 Exhibit 11. Radcliffe Report

3 862. We have one other object in view. This
4 is to strengthen further the research and intelligence
5 side of the Bank's activities and so to assist the Bank
6 to take the lead in promoting and inspiring the objective
7 study of monetary and financial problems. The total
8 volume of research that has been done upon them up to now
9 inside and outside the Bank, appears to us to be in-
10 sufficient. Moreover the additional information that we
11 suggest should be collected will require analysis by
12 experts skilled in its interpretation and able to sift it
13 so as to provide a more comprehensive view of the way in
14 which the different parts of the financial system are
15 functioning. We have suggested that there are certain
16 areas where we are still too much in the dark and where
17 day-to-day decisions have to be taken with only a limited
18 perception of the relevant factors. An increase in the
19 flow of information will help to remedy this; but it will
20 do so more effectively if the information is made the
21 subject of study and research inside the Bank.

22 Exhibit 12. Macmillan Report

23 227.Here we should say at once how
24 strongly we endorse the remarks made in a memorandum of
25 the Canadian Bankers' Association, regarding the vital
26 importance to such an institution of the quality of the
27 governors and directorate. Experience, skill and
28 integrity are required in the highest degree, and that,
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30 be wisely conducted, but also that the institution should



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1 win and maintain the confidence alike of the government,
2 the people and the commercial banks.

3 Exhibit 13. G.F. Towers - House of Commons, 1954.

4 As part of our programme to improve and broaden
5 the money market for the benefit of lenders and borrowers
6 and of our financial structure as a whole, the Bank of
7 Canada has been a constant trader in government of Canada
8 securities since we opened our doors in 1935. While the
9 total amount of our holdings of government securities is
10 necessarily determined by considerations of monetary
11 policy, we have endeavoured to help make a market for all
12 government issues and have been very substantial buyers
13 and sellers. In a sense, we perform a jobbing function,
14 holding the inventories which are indispensable to a good
15 market. Investment dealers and banks also operate in
16 this way, although naturally on a smaller scale. We would
17 be glad to see both dealers and banks extend their oper-
18 ations of this character, and have the Bank of Canada play
19 a smaller part, although we would always expect to be a
20 substantial participant in the market.

21 Exhibit 14. J.E. Coyne - House of Commons, 1956

22 The central bank does not ordinarily take the
23 initiative to increase or decrease the cash reserves of
24 chartered banks. That is to say, it does not step out
25 and bid for securities if it thinks an increase in cash
26 reserves is desirable, or step out and offer securities
27 in the market, if it thinks a decrease in cash reserves
28 is desirable.

29 At any rate, not usually. For the most part
30 there are transactions going on in the market all the



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1 time. People are making offers to buy or to sell, and
2 the central bank is usually in a position to be able to
3 respond to offers to buy from others rather than to take
4 the initiative to make offers itself.

5 When there is a need for more money in the
6 country, you probably find some people -- you are certain
7 to find some people -- are selling securities in order to
8 raise cash. If there is a need for more money as
9 indicated by that fact, the central bank can buy some of
10 those securities that are being offered, and thereby
11 provide the cash. It will probably do so at prices which
12 progressively decline as the strength of the selling
13 pressure keeps up, so that you will probably find rising
14 interest rates at a time when there is a demand for more
15 money.

16 The rise in interest rates, of course, would be
17 much greater if the central bank took no action at all.
18 If we simply stand still interest rates would rise until
19 sufficient buyers were found among the general public to
20 balance the sellers among the general public. So, on the
21 other side of the picture too, when, for a lack of other
22 opportunities to invest, people are interested in buying
23 government securities on an increasing scale the tendency
24 will be for the central bank to provide some of those
25 government securities and sell them, and in that way
26 dampen the fluctuation, which in that case would be a rise
27 in government security prices, and a decline in interest
28 rates. Generally speaking the central bank tries, and
29 I think certainly should try, to foster orderly conditions
30 in markets, and to dampen fluctuations, but not necess-

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1 arily to prevent fluctuations if they represent real
2 changes in supply and demand.

3 Exhibit 15. Radcliffe Report

4 339. At the heart of its work as the central
5 bank lie the Bank's open market operations in Government
6 debt, including both operations in Treasury Bills in the
7 course of management of the money market and operations
8 in Government bonds for the purpose of influencing the
9 gilt-edged market.

10 340. The Bank of England operates almost daily
11 in the money market, by buying Treasury Bills from the
12 market (thus putting cash out) or selling Treasury Bills
13 to the market (thus taking cash in), to smooth out
14 shortages and surpluses of funds between one day and
15 another, which arise mainly out of the uneven incidence
16 of payments by and into the Exchequer. The purpose of
17 these operations is that of maintaining an orderly market
18 It is in the Government's interest, as the
19 largest borrower in the money market, that the money
20 market should be an orderly market; and that requires
21 that the short-term rate of interest should not fluctuate
22 wildly from day to day or week to week but should be
23 reasonably stable.....

24 373.If, for example, the Bank is buying
25 Treasury Bills and selling, in equal amount, short bonds,
26 it is maintaining unchanged the total of the debt but is
27 inducing the private sector to hold the debt with an
28 average maturity date further away: the private sector's
29 total portfolio of financial assets becomes less liquid
30; while if the Bank is selling short bonds or



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339. THE BANK OF ENGLAND

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1 Treasury Bills and buying long bonds, the average
2 maturity of the debt is shortened and the private sector
3 is becoming more liquid.

4 Exhibit 16. P.G. Fousek - Foreign Central Banking

5 In general, the bank appears to confine its
6 open market operations to short-term securities, although
7 on occasion it intervenes also in the medium and long-
8 term market. Partly because data on changes in the
9 detailed composition of the bank's holdings are not
10 published, it is difficult to determine the importance
11 of the bank's longer term operations. In any event, it
12 seems to be agreed by observers that during recent years
13 the bank has conducted operations in longer term
14 securities only in order to smooth out undue deviations
15 from what the authorities have taken to be the underlying
16 trend of securities prices.

17 Exhibit 17. Federal Reserve System Report, 1961.

18 He (Mr. Robertson) also felt that the Committee
19 should return to its previous policy of confining
20 operations to short-term securities. In his view (1) the
21 operation that the Committee had launched in February
22 1961, including transactions in longer-term securities
23 under the special authorization, had not been successful
24 in raising short-term and lowering long-term rates; (2)
25 had the operation been pushed to the point necessary
26 to achieve what he understood to be these twin goals,
27 its defects would not be obvious; and (3) the deleterious
28 effects of such operations on the market for long-term
29 securities will become more apparent when the Treasury
30 seeks -- as it sometime must -- to extend the maturity



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Exhibit 1C. P.G. Tonsak - Foreign Central Banking

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1 structure of the Federal debt by attempting to sell
2 long-term securities for cash or in exchange for maturing
3 securities. Furthermore, he believed that while it was
4 possible for the Federal Reserve to acquire longer-term
5 securities without impeding Treasury operations in a
6 period such as 1961, when Treasury financing was chiefly
7 short-term, the sale of such securities would present
8 real problems. In his view such selling action would
9 not only absorb long-term funds from the limited supply
10 but would also aggravate the uncertainties which already
11 plagued the long-term market, weakening its supporting
12 structure and attenuating its appeal to investors. He
13 could not foresee any time, when monetary policy called
14 for absorbing reserves, that the Federal Reserve could
15 sell longer-term securities from its holdings without
16 impairing the ability of the Treasury to lengthen the
17 debt. This, he thought, would be unfortunate, in view
18 of the real need for the Treasury to achieve a more
19 manageable maturity distribution of the public debt.
20 Accordingly, he believed that operations in securities
21 beyond the short-term area should be terminated
22 immediately.

23 Exhibit 18. Radcliffe Report

24 551.But their attitude has also been
25 strongly influenced by a belief that the long-run
26 interest of the Government as a debtor was best served
27 by orderly markets, and that orderly markets implied
28 abstention from disruption of ruling prices just as much
29 as it demanded official intervention to steady a
30 demoralized market.....A deliberate marking-down of the



Statement of Mr. Robert H. Anderson, Chairman of the Board of Governors of the Federal Reserve System, before the Senate Committee on Banking and Currency, July 1, 1961.

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Exhibit 18. Redcliffe Report

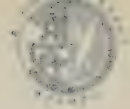
But their attitude has also been strongly influenced by a belief that the long-run interest of the Government as an employer was best served by orderly markets, and that orderly markets implied abstention from disruption of ruling prices just as much as it demanded official intervention to steady a demoralized market.... A deliberate marking-down of the



prices at which the Government broker was willing to sell would have been regarded in the market as arbitrary juggling with the capital values of the Government's own creditors, and this would have seriously damaged "Government credit", at the Government's expense in paying the service of the debt for many years ahead. This "damage to Government credit" would have had repercussions on foreign confidence in sterling: "I need not remind you", the Governor put it, "how closely the exchange markets and the gilt-edged market watch each other".

Exhibit 19. Quest for Stability

The objective of maintaining an orderly market for Government securities was explained more fully in 1939. The purpose was to protect the market from "violent fluctuations of a speculative, or panicky nature" such as that caused by the outbreak of hostilities in Europe. It was not, however, to "assure any given level of prices or yields for Government securities" nor to prevent "an orderly rise or fall in United States bond prices in response to changes in underlying conditions, ".....Recently, there has been another shift of emphasis -- the System adopting the policy that open-market operations should be used for "correcting a disorderly situation in the Government securities market," instead of maintaining an orderly market as formerly. It was felt that the latter policy might result in actions at times which would be in conflict with the over-all goal of helping to maintain economic stability.....



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Exchange Markets and the Gilt-Edged Market

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1 Exhibit 20. R.V. Roosa - Federal Reserve Operations

2 Liaison with the Federal Open Market Committee,
3 is, of course, a two-way street, and it is probably as
4 heavily traveled as the path between any two parts of
5 any unit of Government. The inescapable fact the seat
6 of National Government is in Washington, and that primary
7 responsibility for Federal Reserve policy determination
8 must be in the statutory Federal Open Market Committee
9 which meets in Washington, is paralleled by the equally
10 inescapable fact that the centre of the money market
11 and the Government securities market is in New York.
12 The physical trading facilities and the concentration of
13 skilled trading staffs are also there. Consequently, it
14 has been necessary to work out an unusual variety of
15 arrangements for maintaining continuous contact between
16 Washington, New York and the other Reserve Banks to
17 assure by exchange of information and frequent
18 consultation that the detailed execution of policy in New
19 York is in conformity with the policy objectives
20 developed in Washington by the Committee.

21 Exhibit 21. Hon. D.M. Fleming - House of Commons
22 June 1961 Budget

23 The third announcement I wish to make in the
24 field of debt management concerns the establishment of a
25 purchase fund for the orderly retirement of government
26 debt.....The experience of other governments and of
27 private corporations suggests that the existence of
28 such a fund through which purchases of securities are
29 made can have a steadying effect on the market. Over
30 a period of time it should contribute to a reduction



1 of interest costs.

2 It has therefore been decided to establish a
3 purchase fund to assist in the management of the public
4 debt. Its initial size will be \$100 million, to be
5 used over the next twelve months for the purchase in
6 the market of government of Canada mid and long term
7 securities.

8 Exhibit 22. Hon. D.M. Fleming - House of Commons,
June 1961 Budget.

9 I now return to the exchange rate. As I have
10 said it is the government's intention that our import
11 surplus of goods and services, which has been running in
12 recent years well over a billion dollars annually, should
13 be reduced substantially, and that this should be brought
14 about through an appropriate adjustment of the exchange
15 rate rather than by direct government controls or
16 subsidies, quotas or tariffs.

17 No one can say today what the appropriate level
18 of our exchange rate would be when our balance of pay-
19 ments is in a position better suited to our present
20 economic circumstances. But the rate will certainly
21 be lower than it has been of late, and it may well be
22 appropriate for it to move to a significant discount.
23 It will be government policy to facilitate such a
24 movement.

25 Accordingly the exchange fund will be prepared,
26 as and when necessary, to add substantial amounts to its
27 holdings of United States dollars through purchases in
28 the exchange market. This would have the effect of
29 increasing the foreign exchange reserves available to
30



It has therefore been decided to establish a purchase fund to assist in the management of the public debt. Its initial size will be \$100 million, to be used over the next twelve months for the purchase in the market of government of Canada mid and long term

Exhibit 22. Hon. D.M. Fleming - House of Commons, June 1961 Budget.

I now return to the exchange rate. As I have said it is the government's intention that our imports surplus of goods and services, which has been running in recent years well over a billion dollars annually, should be reduced substantially, and that this should be brought about through an appropriate adjustment of the exchange rate rather than by direct government controls or subsidies, quotas or tariffs.

No one can say today what the appropriate level of our exchange rate would be when our balance of payments is in a position better suited to our present economic circumstances. But the rate will certainly be lower than it has been of late, and it may well be appropriate for it to move to a significant discount. It will be government policy to facilitate such a

Accordingly the exchange fund will be prepared, as and when necessary, to add substantial amounts to the holdings of United States dollars through purchases in the exchange market. This would have the effect of increasing the foreign exchange reserves available to



1 Canada to be used in case of need. As many competent
2 observers have pointed out, these reserves have not grown
3 over the past decade in line with Canada's international
4 transactions. Once an exchange rate more closely in line
5 with Canada's economic position is achieved, the
6 government will use the resources of the exchange fund
7 to ensure that the rate is kept within a range appropriate
8 to Canada's changing economic situation.....

9 Exhibit 23. W.E. McLaughlin, 1962

10 From September, 1950, to December 1960, Canada
11 had a true floating exchange rate, in the sense that,
12 aside from smoothing operations through the Exchange Fund
13 Account, its value was determined entirely by demand and
14 supply in the market.

15 From the "baby budget" of December 20, 1960
16 to June 20, 1961, this true floating rate was abandoned
17 in favour of what we might call a nudged floating rate.
18 There was no announcement of a change in policy but the
19 Exchange Fund did exert downward pressure on the Canadian
20 dollar through the purchase of U.S. dollars in the open
21 market.

22 With the final budget, brought down on June 20,
23 1961, a third variety of floating rate appeared with
24 the announcement that in the Government's view the rate
25 should move to a "significant discount"; but there was
26 no definition of the term "significant" and no clear
27 indication, therefore, of the amount of discount that
28 would be regarded as satisfactory. The uncertainty
29 created by this announcement thinned out both sides
30 of the market and the net result was that the Canadian



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1 dollar settled to a discount position without initially
2 requiring active intervention by the Exchange Fund.

3 However, since that time the Government has,
4 through public announcement or use of the Exchange Fund,
5 actively intervened in the market whenever it has chosen
6 to do so, and the nudged floating rate has clearly given
7 way to a manipulated floating rate.

8 Hon. Donald M. Fleming, House of Commons, April 1962,
9 Budget.

10 Since 1950 the Government, using the Exchange
11 Fund which was set up in 1935, has operated to restrain
12 and smooth out the more rapid movements of the rate in
13 one direction or the other. At no time, throughout the
14 whole period, have the resources of the Exchange Fund been
15 used aggressively, to push the rate in one direction or
16 the other against market forces.....

17 The Government has not hesitated, and will not
18 hesitate in the future, to deploy a substantial volume
19 of funds, on one side of the market or the other, in
20 order to prevent sudden or erratic movements in our
21 exchange rate.

22 R.V. Roosa, 1962 Speech.

23whether a country formally adheres to the
24 gold standard or not, it must have a reserve of some
25 kind of internationally acceptable purchasing power --
26 either gold or dollars, or possibly pounds sterling, or
27 an equally usable quick line of credit. Whenever its
28 current receipts from sales or the inflow of capital do
29 not equal its current outpayments, it has to draw on
30 this reserve. Consequently, the size and ready usability

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1 of the reserve -- together with the quick claims against
2 it -- must be watched continually as an indication of
3 changes in each country's external economic strength or
4 weakness.

5 No country can pursue policies indefinitely
6 which consume its external reserves and draw down its
7 potential credit abroad.

8a fixed link must be preserved between
9 gold -- the universal monetary metal of timeless
10 acceptability -- and at least one national currency.
11 Since the mid-thirties, the dollar alone has served that
12 function. It is essential that the United States
13 continue freely buying gold, and selling it to the
14 monetary authorities of the world, at the price of \$35
15 per fine ounce....all leading countries (must) maintain
16 fixed (rather than variable) rates of exchange in
17 relation to the dollar, with narrow permissible spreads
18 around the declared par value -- such as the 1 per cent,
19 each way, established by the International Monetary Fund.
20 There must be room for market forces to demonstrate,
21 through small changes within such a band, whether a given
22 currency is presently strengthening or weakening. But
23 there must not be an escape hatch through which one
24 country or another can seek temporary refuge from
25 balance-of-payments disciplines by juggling its own
26 exchange rate -- beggaring its neighbours and disrupting
27 the orderly process of cost and price adjustment among
28 the various products and services that are required for
29 eventual balance-of-payments equilibrium.



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1 Exhibit 24. Bank Reserves

2 The preoccupation by the banking community
3 with changes in reserve requirement percentages in recent
4 years has tended to obscure the primary function of the
5 required reserve in the regulation of bank credit and
6 the money supply. This dominant function is to provide
7 a fulcrum on which a flexible monetary policy can get
8 leverage and effectiveness. Since a specific volume of
9 reserves must be held by member banks against their
10 deposit liabilities, the Federal Reserve System, by sell-
11 ing Government securities, can absorb banks' excess or
12 marginal reserves, which are available as the basis for
13 credit expansion, or can force member banks to borrow
14 to maintain their required reserves. Thus the System
15 can influence the banks' ability and willingness to extend
16 additional credit. Similarly, by buying Government
17 securities the System can provide the banks with funds
18 with which to repay their indebtedness or to accumulate
19 free reserves, on the basis of which they can make
20 additional loans or investments.

21 Exhibit 25. G.F. Towers - House of Commons, 1954.

22 There is a risk that the central bank will use
23 that power as a crutch with which to obviate or perhaps
24 postpone the broader action in the field of monetary
25 policy which would really be appropriate....But I believe
26 that if it used those powers to supplement its other
27 actions....the power can be very useful, provided it is
28 carefully used and seldom used and never simply as a
29 crutch....I would hope that the power....would only be
30 exercised at a time of sudden need and that as quickly

The preoccupation by the banking community with changes in reserve requirement percentages in recent years has tended to obscure the primary function of the required reserve in the regulation of bank credit and the money supply. This dominant function is to provide a fulcrum on which a flexible monetary policy can get leverage and effectiveness. Since a specific volume of reserves must be held by member banks against their deposits, the Government securities, can absorb banks' excess or marginal reserves, which are available as the basis for credit expansion, or can force member banks to borrow to maintain their required reserves. Thus the System can influence the banks' ability and willingness to expand additional credit. Similarly, by buying Government securities the System can provide the banks with funds with which to repay their indebtedness or to accumulate free reserves, on the basis of which they can make additional loans or investments.

There is a risk that the central bank will use that power as a crutch with which to obviate or perhaps postpone the broader action in the field of monetary policy which would really be appropriate.... But I believe that if it used those powers to supplement its other actions... the power can be very useful, provided it is carefully used and seldom used and never simply as a crutch.... I would hope that the power... would only be exercised at a time of sudden need and that as quickly



1 as possible after that we would get back to the 8 per
2 cent ratio.....I think that the main purpose would be
3 to hold the level in a substantial inflationary spurt
4 without having to rely completely and suddenly on
5 activities in the securities market.

6 Exhibit 26. J.B. Coyne - 1955 Report

7 In the course of discussions with the chartered
8 banks in November and December the Bank of Canada urged
9 the adoption of a standard practice regarding the
10 maintenance of a minimum ratio of liquid assets (cash,
11 day-to-day loans and treasury bills) to deposits. The
12 purpose of this suggestion was to establish a working
13 principle of bank operations which would help the
14 central bank in the task of restraining inflationary
15 pressures that might threaten in the future.

16 The function of a minimum liquid asset ratio
17 is to increase the effectiveness of monetary policy in
18 moderating a too rapid expansion of credit, by bringing
19 the influence of monetary restraint to bear on the
20 lending policies of the banks, on interest rates, and
21 on security markets generally, earlier and more gradually
22 and with greater certainty than would otherwise be the
23 case.....

24 After discussion, the banks have agreed to
25 work to achieve by May 31st, 1956, a minimum liquid asset
26 ratio of 15 per cent which they will endeavour to maintain
27 on a daily average basis from June on. On this basis,
28 fluctuations above or below 15 per cent may occur from
29 day to day or week to week, but for the month as a whole
30 the average would not be below the target ratio.....



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Memorandum of Understanding - 1956

In the course of discussions with the chartered banks in November and December the Bank of Canada urged the adoption of a standard practice regarding the maintenance of a minimum ratio of liquid assets (cash, day-to-day loans and treasury bills) to deposits. The purpose of this suggestion was to establish a working principle of bank operations which would help the central bank in the task of restraining inflationary pressures that might threaten in the future.

The function of a minimum liquid asset ratio is to increase the effectiveness of monetary policy in moderating a too rapid expansion of credit, by bringing the influence of monetary restraint to bear on the lending policies of the banks, on interest rates, and on security markets generally, earlier and more gradually and with greater certainty than would otherwise be the case.....

After discussion, the banks have agreed to work to achieve by May 31st, 1956, a minimum liquid asset ratio of 15 per cent which they will endeavour to maintain on a daily average basis from June on. On this basis, fluctuations above or below 15 per cent may occur from day to day or week to week, but for the month as a whole the average would not be below the target ratio.....



1 Exhibit 27. James Muir - 1958

2 With the inception of a tighter money policy
3 some two years ago, it was arranged between the Bank of
4 Canada and the chartered banks that the latter would
5 maintain a secondary reserve of 7 per cent of Canadian
6 deposit liabilities in day-to-day loans and Government
7 Treasury Bills. The maintenance of secondary reserves
8 by the banks was nothing new; the innovation lay in
9 stating reserve requirements in terms of a positive
10 objective.

11 What we have now to avoid is that this
12 objective should become an inflexible figure. An
13 inflexible reserve is not in fact a reserve at all but
14 a compulsory investment.

15 Exhibit 28. R.V. Roosa - Federal Reserve Operations

16 The use of the "discount window" by member banks
17 is, of course, a privilege that is not to be abused or
18 overused, since no bank should expect to exist on
19 permanently borrowed capital beyond the equity supplied
20 by its own shareholders.....the "discount window" is not
21 a loophole in the Federal Reserve System's credit control
22 apparatus. It is instead a safety valve, enabling
23 individual banks to restore their reserves to the
24 required level when unforeseen losses of funds have
25 created reserve deficiencies,In effect, borrowing
26 gives the affected bank time both to determine whether or
27 not fundamental changes will have to be made in its own
28 portfolio and to carry out in a reasonably orderly
29 manner any such changes that prove to be necessary.....

30 Supplementing the borrowing of the banks, which

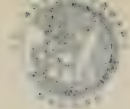


Exhibit 27. James Muir - 1958

With the inception of a tighter money policy some two years ago, it was arranged between the Bank of Canada and the chartered banks that the latter would maintain a secondary reserve of 7 per cent of Canadian deposits in day-to-day loans and government Treasury Bills. The maintenance of secondary reserves by the banks was nothing new; the innovation lay in stating reserve requirements in terms of a positive objective.

What we have now to avoid is that this objective should become an inflexible figure. An inflexible reserve is not in fact a reserve at all but a compulsory investment.

Exhibit 28. R.V. Brown - Federal Reserve System

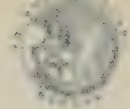
The "discount window" of central banks is, of course, a privilege that is not to be abused or overused, since no bank should expect to exist on permanently borrowed capital beyond the equity supplied by its own shareholders.... the "discount window" is not a loophole in the Federal Reserve System's credit control apparatus. It is instead a safety valve, enabling individual banks to restore their reserves to the required level when unforeseen losses of funds have created reserve deficiencies. In effect, borrowing gives the affected bank time both to determine whether or not fundamental changes will have to be made in its own portfolio and to carry out in a reasonably orderly manner any such changes that prove to be necessary. Supplementing the borrowing of the banks, which



1 is always at the initiative of the banks themselves,
2 and which is always granted initially (perhaps with rate
3 exceptions, in circumstances that would have been already
4 discussed with an offending bank), there is an entirely
5 different method of providing funds which the Federal
6 Reserve also may use in smoothing the gyrations of the
7 money market -- that is, the repurchase agreement with
8 non-bank Government securities dealers. Under a re-
9 purchase agreement, the Federal Reserve acquires
10 securities from a dealer against payment, under a
11 contract which binds the dealer to repurchase the same
12 securities at the same price on or before a stipulated
13 final date, and to pay the Federal Reserve a specified
14 rate of interest over a period that it holds the
15 securities.

16 Exhibit 29. Bank of Canada Discount Rate Changes

17 <u>Date</u>	18 <u>Rate</u>	19 <u>Comment</u>
20 March 21 11, 1935	22 $2\frac{1}{2}\%$	23 Our bank rate was established at $2\frac{1}{2}\%$ per 24 cent and remains unchanged. The figure is the 25 same as that which was being charged for 26 advances under the Finance Act, prior to the 27 establishment of the Bank of Canada, and it 28 remains the charge which we would ordinarily 29 make to the banks for advances. It is quite 30 out of touch with Treasury Bill rates, but this fact is not at present of any particular significance. When money is in plentiful supply, the need for loans or rediscount facilities seldom arises. It is in times of greater stringency that accommodation from the



is always at the initiative of the banks themselves, and which is always granted initially (perhaps with rate exceptions, in circumstances that would have been already discussed with an offending bank), there is an entirely different method of providing funds which the Federal Reserve also may use in smoothing the gyrations of the money market -- that is, the repurchase agreement with non-bank Government securities dealers. Under a repurchase agreement, the Federal Reserve acquires securities from a dealer against payment, under a contract which binds the dealer to repurchase the same securities at the same price on or before a stipulated final date, and to pay the Federal Reserve a specified rate of interest over a period that it holds the

Exhibit 29. Bank of Canada Discount Rate Changes

Date	Rate	Comment
March 11, 1935	2 1/2%	Our bank rate was established at 2 1/2 per cent and remains unchanged. The figure is the same as that which was being charged for advances under the Finance Act, prior to the establishment of the Bank of Canada, and it remains the charge which we would ordinarily make to the banks for advances. It is quite out of touch with Treasury Bill rates, but this fact is not at present of any particular significance. When money is in plentiful supply, the need for loans or rediscount facilities seldom arises. It is in times of greater stringency that accommodation from the

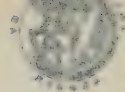


central bank is essential. A central bank must be what is known as the lender of last resort, which implies that in times of real need its rediscounting and lending facilities will be freely accorded.

Reference - First Annual Meeting of the Shareholders of the Bank of Canada, February 25, 1936, page 16.

February 7, 1944 1½% At a meeting of the Board of Directors on February 7th, 1944, it was decided to reduce

the Bank Rate to 1½ per cent, effective February 8th, from the 2½ per cent level which had been maintained since the Bank's establishment in 1935. During the intervening period, there had been a considerable reduction in interest rates on short-term securities, and the bank rate was somewhat out of line with the current market. However, this was not a matter of great importance because the lending facilities of the Bank have been required on few occasions and for rather small amounts. The change to a 1½ per cent rate does not mean that the Bank expects its credit facilities to be needed on a much greater scale in the future than in the past. Nor does it mean that under the existing war conditions there is any less need for people to save. The utmost effort to maintain and increase our saving is still necessary, and the first and foremost concern of financial policy must be with winning the



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At a meeting of the Board of Directors on February 7th, 1944, it was decided to reduce the Bank Rate to $1\frac{1}{2}$ per cent, effective February 8th, from the $2\frac{1}{2}$ per cent level which had been maintained since the Bank's establishment in 1935. During the intervening period, there had been a considerable reduction in interest rates on short-term securities, and the bank rate was somewhat out of line with the current market. However, this was not a matter of great importance because the lending facilities of the Bank have been reduced on few occasions and for rather small amounts. The change to a $1\frac{1}{2}$ per cent rate does not mean that the Bank expects its credit facilities to be needed on a much greater scale in the future than in the past. Nor does it mean that under the existing war conditions there is any less need for people to save. The utmost effort to maintain and increase our saving is still necessary, and the first and foremost concern of financial policy must be with winning the



war. The stage has now come, however, when many are also having to give thought to the economic problems which will arise after the war.

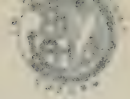
One factor which will affect decisions is the prospective cost of borrowing. It therefore seems appropriate that the Bank should, by reducing its Rate, signify its intention to continue the kind of monetary policy which has brought about the current level of interest rates. A policy aimed at higher interest rates would only become intelligible if, after war shortages are over, consumers' expenditure and capital development were to proceed at a rate which would overstrain our productive capacity. I see no prospect of such a situation arising in a form which would call for a policy of raising interest rates.

Reference - Report of the Governor of the Bank of Canada to the Minister of Finance for 1943, pages 4-5.

October 2% Effective October 17th Bank Rate was increased 17, 1950

ed from $1\frac{1}{2}$ per cent to 2 per cent per annum.

The $1\frac{1}{2}$ per cent rate had been in effect from February 8th, 1944, prior to which date the rate had been $2\frac{1}{2}$ per cent. The Bank issued a press release on October 16th containing the following statement: "At the time the reduction in Bank Rate took place in 1944, the Bank expressed the view that it did not then see any



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Reference - Report of the Governor of the Bank

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for 1943, pages 4-5.

October 17, 1943

2% Effective October 15th Bank Rate was increased

from 1 1/2 per cent to 2 per cent per annum.

The 1 1/2 per cent rate had been in effect from

February 8th, 1944, prior to which date the

rate had been 2 1/2 per cent. The Bank issued a

press release on October 16th containing the

following statement: "At the time the reduc-

tion in Bank Rate took place in 1944, the Bank

expressed the view that it did not then see any



prospect of an economic situation in the post-war period of a character which would call for a policy of raising interest rates. The change to a 2 per cent Bank Rate is an indication that the earlier view no longer holds good under today's conditions when Canada faces the prospect of substantially increased defence expenditures adding to the pressure on the country's resources at a time of virtually full employment."

Reference - Report of the Governor of the Bank of Canada to the Minister of Finance for 1950, pages 12-13.

February 14, 1955

1½% The Bank of Canada announced at the close of business today a reduction in "Bank Rate" to 1½ per cent from the previous level of 2½ per cent which was established in October 1950. The Bank Rate is the minimum rate at which the central bank will lend for short periods to the chartered banks and the money market on the security of Treasury Bills and short-term Government bonds. Yields on these securities have declined materially over the past year and a half and Bank Rate at the old level had ceased to bear a reasonable relationship to other short-term interest rates.

In the past, Bank Rate has been changed infrequently in Canada and little use has been made of the Bank's facilities. The growth in the breadth and scale of activity in the short-term money market over the past two years has made



prospect of an economic situation in the post-war period of a character which would call for a policy of raising interest rates. The change to a 2 per cent Bank Rate is an indication that the earlier view no longer holds good under today's conditions when Canada faces the prospect of substantially increased defence expenditures adding to the pressure on the country's resources at a time of virtually full employment."

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In the past, Bank Rate has been changed infrequently in Canada and little use has been made of the Bank's facilities. The growth in the breadth and scale of activity in the short-term money market over the past two years has made



it desirable that the Bank rate to be made more flexible and bear a closer (though not fixed) relation to other short-term interest rates.

The present adjustment will help to make Bank Rate a more significant factor in the money market and facilitate its more flexible use in the future as circumstances may require.

While the structure of short-term interest rates, including Bank Rate, provides an index of monetary conditions, it does not follow that every change in Bank Rate or in the level of other short rates necessarily indicates a change in general economic conditions.

Reference - Statement from Bank of Canada, dated February 14, 1955.

August 5, 1955 2%

October 12, 1955 $2\frac{1}{4}\%$

November 18, 1955 $2\frac{3}{4}\%$

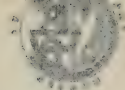
April 4, 1956 3%

August 9, 1956 $3\frac{1}{4}\%$

October 17, 1956 $3\frac{1}{2}\%$

November 1, 1956 Floating Rate Since the Bank of Canada acts in

the role of lender of last resort, its lending rate should not be as low as the interest rate on the most liquid form of security in the market, namely treasury bills... Prior to November 1st, 1956 the Bank had follow-



Prior to November 1st, 1950 the Bank had followed security in the market, namely treasury bills... interest rate on the most liquid form of its lending rate should not be as low as the



ed the practice of keeping its lending rate above the treasury bill rate by raising the Bank Rate at intervals of some months whenever the treasury bill rate approached or temporarily exceeded the previous level of the Bank Rate. In 1956 the Bank Rate was increased from $2\frac{3}{4}$ per cent to 3 per cent on April 4th, to $3\frac{1}{4}$ per cent on August 9th and to $3\frac{1}{2}$ per cent on October 17th. This procedure gave rise to some misunderstanding; in some quarters it was apparently thought that the central bank was setting or fixing or controlling interest rates of all kinds by its action in changing and publishing its own minimum lending rate. The simplest method of ensuring that the Bank Rate will always be higher than the treasury bill rate is to keep it at some specified and published margin above the treasury bill rate, whatever the latter may be. This method was adopted on November 1st when the Bank announced that it would thereafter until further notice adjust its lending rate once a week in order to maintain it at a level of $\frac{1}{4}$ of 1 per cent above the average rate on treasury bills at the most recent tender or auction of treasury bills. At the close of the year the Bank Rate was 3.92 per cent. Another reason for adopting the new method of determining the Bank Rate was that weekly changes in the treasury bill rate are relatively

of the practice of keeping its lending rate above the treasury bill rate by raising the Bank Rate at intervals of some months whenever the treasury bill rate approached or temporarily exceeded the previous level of the Bank Rate. In 1926 the Bank Rate was increased from 2 $\frac{3}{4}$ per cent to 3 per cent on April 14th, to 3 $\frac{1}{2}$ per cent on August 9th and to 3 $\frac{3}{4}$ per cent on October 15th. This procedure gave rise to some misunderstanding; in some quarters it was apparently thought that the central bank was setting or fixing or controlling interest rates of all kinds by its action in changing and publishing its own minimum lending rate. The simplest method of ensuring that the Bank Rate will always be higher than the treasury bill rate is to keep it at some specified and published margin above the treasury bill rate, whatever the latter may be. This method was adopted on November 1st when the Bank announced that it would thereafter wait further notice adjust its lending rate once a week in order to maintain it at a level of $\frac{1}{4}$ of 1 per cent above the average rate on treasury bills at the most recent tender or auction of treasury bills. At the close of the year the Bank Rate was 3.92 per cent.

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1 small in either direction and the fact that
2 such changes occur weekly has become well under-
3 stood. On the other hand, unexpected, unpre-
4 dictable, infrequent and relatively large
5 changes in the Bank's lending rate under the
6 previous system were known to have a disturbing
7 effect on business in general and on all
8 persons who might be contemplating the making
9 of investments or entering into business arrange-
10 ments involving credit and rates of interest.
11 No difficulties of this sort have been reported
12 since the adoption of the new system.

13 Reference - Report of the Governor of the Bank
14 of Canada to the Minister of Finance
15 for 1956, pages 45-46.

16 In his Report for 1960, Mr. Coyne, in an
17 apparent effort to justify the continuance of the floating
18 rate, traced the history of the Bank's discount rate and
19 compared its use with the use made of such facilities in
20 the United Kingdom and the United States. Pages 58-64.

21 Exhibit 30. James Muir - 1958

22I can add only that I wish Bank Rate were
23 a more positive thing -- that it should assume the more
24 manly role of being a leader rather than create the
25 impression of meekly following money market operations.

26 James Muir, 1960.

27there is need for improved communication
28 between the Bank of Canada and the chartered banks. Of
29 course, communication must be a two-way street. I have
30 long deplored the passing of bank rate in Canada from the

small in either direction and the fact that such changes occur weekly has become well under

standards, and the only real difficulty is

disturbance, infrequent and relatively large changes in the Bank's lending rate under the previous system were known to have a disturbing

effect on business in general and on all

persons who might be contemplating the making

of investments or entering into business arrangements

with the Bank. The fact that the Bank's

No difficulties of this sort have been reported

under the present system is a very good indication

of the success of the new system.

of Canada to the Minister of Finance.

and from the Bank.

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apparent effort to justify the continuance of the floating

rate, traced the history of the Bank's discount rate and

compared its use with the use made of such facilities in

the United Kingdom and the United States. Pages 52-64.

Exhibit 10 - 1960-1961

.....I can add only that I wish Bank Rate were

a more positive thing -- that it should assume the more

many role of being a leader rather than create the

impression of meekly following money market operations.

There will, I think,

.....there is need for improved communication

between the Bank of Canada and the chartered banks. Of

course, communication must be a two-way street. I have

long deplored the passing of bank rate in Canada from the



1 of communication in this sense to a mere shadow, floating
2 $\frac{1}{4}$ per cent above the market rate for three month Treasury
3 Bills. However, we must respect the Bank of Canada's
4 evident determination to avoid even the possibility of a
5 modest departure from the collective judgment of the free
6 market.

7 Fortunately, the chartered banks are not yet
8 reduced to the interpreting of obscure signs and port-
9 ents or the reading of entrails to divine Bank of Canada
10 policy; although a cynic might suggest that we have
11 progressed very little beyond the plight of the noble
12 savage watching as in olden times for the occasional smoke
13 signal from the haughty Ottawas.

14 G. Arnold Hart - 1960

15 The need for what might be termed a lead from the
16 central monetary authorities is all the more apparent by
17 reason of the curious method by which the central bank's
18 rediscount rate is determined. In other money markets a
19 change in the rediscount rate is rightly regarded as a
20 matter of the highest significance. It traditionally
21 represents a means by which central bank indicates to the
22 market its views as to whether credit should become more
23 stringent or more plentiful. In Canada, by contrast,
24 the rediscount rate, since November 1956, has been
25 determined weekly by the expedient of adding a quarter of
26 one per cent to the average weekly tender rate for three-
27 month treasury bills. In other words, what in other
28 money markets is a major monetary indicator that is
29 changed infrequently and only in the light of official
30 reappraisal of fundamental conditions, is in Canada like



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reappraisal of fundamental conditions, is in Canada like



1 a cork that bobs around from week to week.....

2 J. Douglas Gibson - 1960

3A clearer indication from the central bank
4 to the business community as to the direction of its
5 monetary thinking would therefore be helpful in promoting
6 more stable financial conditions and perhaps in encourag-
7 ing a level of long-term interest rates less restrictive
8 to the potential borrower.

9 It is often said that we should return to the
10 traditional system of having the central bank formally
11 set the Bank Rate from time to time. The automatic
12 system has been tried and, whatever its merits, it rules
13 out the possibility of giving any signal or direction to
14 the financial community. I think on balance it might
15 be useful to restore the Bank Rate signal.....

16 Quest for Stability

17Changes in the discount rate, as a symbol
18 of Federal Reserve policy, may have important psycholog-
19 ical effects. They reflect the recognition by a group of
20 well-informed and responsible officials of a change in
21 the credit situation. An increase in the rate indicates
22 official concern over credit expansion and points toward
23 a tighter credit policy. A decrease may be regarded as
24 an indication of an easier credit policy and possibly
25 lower interest rates.....

26 Exhibit 31 - J.E. Coyne - 1956 Report

27 Finance companies carry on an operation which
28 is in all essentials banking, but are not restrained by
29 changes in monetary conditions. They are able to compete
30 for deposits through the sale of short-term paper in the



a cork that pops around from week to week.....

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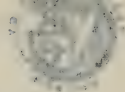


1 money market and to raise funds in securities markets,
2 paying any necessary rate of interest for these purposes,
3 for increased interest costs do not appear to deter con-
4 sumer borrowing. Banks may not charge more than 6 per
5 cent interest on loans. Finance companies are not limited
6 in this respect and their rates of interest on carrying
7 charges range from 1 per cent to 2 per cent per month,
8 i.e. 12 per cent to 24 per cent per year, or more. Some
9 of the companies are subsidiaries of large foreign
10 corporations and can obtain funds directly from them.
11 Finance companies are not required to maintain reserves
12 nor are they subject to regulation in the way that banks,
13 life insurance companies and some other investment
14 institutions are.

15While consumer credit may be a useful
16 adjunct of modern merchandising, large fluctuations in
17 the volume of such credit make it a de-stabilizing factor
18 working against the stabilizing efforts of fiscal and
19 monetary policy. The existence of what amounts to a
20 rival banking system, competing for deposits and short-
21 term funds in order to make short-term loans to finance
22 consumption.....without supervision or regulation, and
23 out of step with the trend of credit policy in the regular
24 banking system, can be a definite handicap to monetary
25 policy during a boom.....

26 James Muir - 1957.

27 The second source of additional inflationary
28 pressure is the result of the growth of non-bank
29 repositories of funds. Some of these are subject to
30 governmental regulation or control, but not by our



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i.e. 12 per cent to 24 per cent per year, or more. Some
of the companies are subsidiaries of large foreign
corporations and some have foreign capital.
Finance companies are not required to maintain reserves
nor are they subject to regulation in the way that banks
are. The Federal Reserve Board has issued regulations
governing the activities of finance companies.

....While consumer credit may be a useful
adjunct of modern merchandising, large fluctuations in
the volume of such credit make it a destabilizing factor
working against the stabilizing efforts of fiscal and
monetary policy. The existence of what amounts to a
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James Malt - 1957.

The Federal Reserve Board is particularly interested
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monetary authorities and not for purposes appropriate to monetary policy.

The curtailment of bank credit may have little direct effect on the supply of funds from non-bank sources. Even those institutions, such as the finance companies, with traditionally large bank loans, have alternative sources of funds, and these sources become more significant as the non-bank sector of the business community increases in importance as a repository of liquid funds.

It would seem therefore, to be at least open to doubt whether the present facilities and techniques available to our monetary authorities are sufficiently wide in scope to deal with present-day problems of credit control. The classical weapon -- upward movement of interest rates, largely through commercial banks -- may by itself prove an impotent policy. The "bite" applied can seize upon an insufficiently large segment of the whole money and credit system. Over the years, such an abundance of other forms of credit creation has arisen that the over-all supply of credit may move in a direction completely opposite to that which official monetary policy is trying to induce. It may be taking too positive a view of a distant scene, but it would at least appear that, in order to be fair and in order to achieve the best results, our monetary and credit control may have to embrace a wider area of our financial world than it now does.

James Muir - 1960.

The implication of this ambiguity for policy is

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James Mait - 1950.

The implication of this ambiguity for policy is



1 simply this, that monetary control is inhibited and may
2 at times be ineffective, as well as inequitable, in
3 controlling the money supply in this broader sense.
4 Rather than extend the range of specific government
5 regulation, it might be worthwhile to require that these
6 lenders (who, in effect, do a banking business so far as
7 the total supply of money and credit is concerned) should,
8 like the chartered banks, be subject to appropriate cash,
9 or other, reserve requirements.

10 Exhibit 32. G.F. Towers - 1936 Report.

11 I believe that it was a wise move on the part
12 of the leading Canadian Stock Exchanges to raise margin
13 requirements during 1936, and I feel sure that they will
14 have the co-operation of other lenders if -- as may well
15 be the case -- further increases become necessary.

16 G.F. Towers - House of Commons, 1944

17 I think it was in 1936 -- although I am speaking
18 from memory -- that it seemed to us that the very active
19 and rising stock markets which were in existence at that
20 time were tending to go a shade too far in their use
21 of increased credit. So that we did speak to the
22 committees of the stock exchanges and also to the banks,
23 and suggested that the percentage of margin requirements
24 should be raised. That was a matter of suggestion and
25 persuasion; but it did not take anything very much in
26 that way, because I think that the banks and the
27 committees of the stock exchanges agreed that would be a
28 wise move, and it was done.

29 Exhibit 33. G.F. Towers - 1946 Report

30 In the case of Canada where the chartered banks



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In the case of Canada where the chartered banks



1 carry on both savings and commercial banking under one
2 roof, an agreement was made with the government early in
3 1946 recognizing the link between savings deposits and
4 holdings of market issues of government securities. The
5 banks agreed that their investments in Dominion government
6 direct and guaranteed issues (other than Treasury Bills,
7 Deposit Certificates and Treasury Notes) would not average
8 more than 90 per cent of the amount of their Canadian
9 personal savings deposits. The banks also agreed that
10 their earnings on such bonds should not exceed the cost of
11 operating their savings business by more than a moderate
12 profit margin.

13 Exhibit 34. G.F. Towers - 1948 Report.

14 Before 1945, chartered banks seldom financed
15 business capital expenditures through medium or long term
16 loans. In the post-war period, however, the chartered
17 banks extended a substantial amount of capital assistance
18 to business through the purchase of corporate securities,
19 particularly in 1947. Early in 1948 it became apparent
20 that business intended to make even larger capital
21 expenditures and that this might mean increased pressure
22 on available labour and materials. Accordingly, the Bank
23 in February 1948 suggested to the chartered banks that
24 conditions prevailing at that time made it undesirable for
25 capital expenditures to be financed through expansion of
26 bank credit. We suggested that it would be preferable
27 for borrowers to obtain such funds by the sale of
28 securities to the public, except in the case of those
29 borrowers, mainly small concerns, for whom a public issue
30 would not be an appropriate means of financing.

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1 Exhibit 35. G.F. Towers - 1951 Report

2 Meetings with representatives of the chartered
3 banks during February 1951 to discuss the situation found
4 the banks in agreement with the suggestion that further
5 expansion in total bank credit was undesirable under
6 existing conditions. To prevent such a development the
7 banks undertook a more rigorous scrutiny of applications
8 for credit with a view to curtailing advances for less
9 essential purposes and to encourage borrowers to go to
10 the security market or elsewhere for their capital require-
11 ments.

12 Exhibit 36. J.E. Coyne - 1955 Report.

13 Historically, in their role as commercial
14 bankers, the chartered banks have not made a practice of
15 term lending, that is, making loans to business corporat-
16 ions where the time of payment is deferred beyond that
17 of ordinary bank loans, or purchasing a security issue
18 negotiated directly with the customer as distinct from
19 buying a publicly issued security in the market. In
20 recent years, however, term lending has appeared in three
21 distinct periods, with little such lending taking place
22 in the intervals between. On each occasion the Bank of
23 Canada has felt it necessary to propose and the banks
24 have agreed to a cessation of most forms of term lending.
25 The first occasion was from January 1948 to February 1949.
26 The second occasion was from February 1951 to May 1952,
27 this time in conjunction with a general ceiling on all
28 forms of bank loans. The third such occasion came during
29 1955.

30 In September I discussed with the banks the

Exhibit 35. G.F. Towers - 1951 Report

Meetings with representatives of the chartered banks during February 1951 to discuss the situation facing the banks in agreement with the suggestion that further expansion in total bank credit was undesirable under existing conditions. To prevent such a development the banks undertook a more rigorous scrutiny of applications for credit with a view to curtailing advances for less essential purposes and to ensure that the security market or elsewhere for their capital requirements.

Exhibit 36. L.E. Coyne - 1955 Report

Historically, in their role as commercial bankers, the chartered banks have not made a practice of term lending, that is, making loans to business corporations where the time of payment is deferred beyond that of ordinary bank loans, or purchasing a security issue negotiated directly with the customer as distinct from buying a publicly issued security in the market. In recent years, however, term lending has appeared in three distinct periods, with little such lending being placed in the intervals between. On each occasion the Bank of Canada has felt it necessary to propose and the banks have agreed to a cessation of most forms of term lending. The first occasion was from January 1941 to February 1942. The second occasion was from January 1945 to February 1946. This time in conjunction with a general ceiling on all forms of bank loans. The third such occasion came during In September I discussed with the banks the



1 rapid increase which appeared to be taking place in their
2 term lending to corporations. In order that both the Bank
3 of Canada and the chartered banks would be in a better
4 position to appraise the situation, a weekly report from
5 each bank of the amount of its forward commitments in
6 respect of term lending....was instituted..... At the
7 end of November it was agreed that all banks would in
8 general cease making new commitments for term lending.

9 The agreement to refrain from term lending, as
10 defined, does not prevent the banks from extending
11 temporary credit to their customers for capital develop-
12 ment programmes.....

13 Exhibit 37. J.E. Coyne - 1956 Report

14 Another step taken by the Bank with a view to
15 reducing if possible outstanding anomalies was in
16 connection with stock market credit required for margin
17 trading. Increases in the amount of credit used for this
18 purpose in the United States had prompted the Federal
19 Reserve Board to exercise its powers to increase margin
20 requirements from the previous level of 50 per cent, to
21 60 per cent in January 1955 and 70 per cent in April 1955,
22 a requirement which is still in force. As a result, the
23 total volume of credit used for stock market trading did
24 not significantly increase in the United States after
25 April 1955. In Canada, on the other hand, the volume
26 of credit so used had approximately doubled between March
27 1955 and July 1956. The general margin requirement
28 according to the rules of the stock exchanges in Canada is
29 50 per cent. The Bank of Canada has no power to impose
30 or alter margin requirements. The Bank did, however, have



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Exhibit 37. J.R. Goyne - 1956 Report

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1 a discussion with members of the governing bodies of the
2 Montreal, Canadian and Toronto Stock Exchanges, in the
3 course of which general agreement was expressed that it
4 would be undesirable for the volume of credit used in
5 stock trading to increase any further under present
6 conditions.....

7 Exhibit 38. J.E. Coyne - 1956 Report

8 Again, it became apparent during 1956 that the
9 volume of consumer credit, particularly in the form of
10 instalment finance, was expanding more rapidly than other
11 forms of credit, such as ordinary bank loans, and was
12 continuing to expand rapidly in the latter part of the
13 year after bank credit had more or less levelled off.
14 The Bank held discussions with representatives of the
15 major instalment finance companies with a view to seeing
16 whether some voluntary agreement could be reached among
17 the leaders of the industry to prevent any further
18 significant increase in the total volume of credit of
19 this character. It turned out that agreement of all
20 concerned could not be reached.....The Bank also had an
21 informal discussion with representatives of the major
22 department stores and chain stores engaged in selling
23 consumers' durable goods on credit, many of which do
24 their own financing but also depend on occasion upon funds
25 provided by the instalment finance companies. These
26 representatives expressed the view that in their business
27 credit terms had not been relaxed, and no agreement was
28 reached with respect to restraining further increase in
29 the volume of consumer credit extended through these
30 outlets.....

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1 Exhibit 39. J.E. Coyne - 1957 Report

2 In the early months of 1957 the chartered banks
3 had virtually withdrawn from the field of insured
4 residential mortgage lending.....

5 In discussing this situation with the chartered
6 banks I expressed the view that they should maintain
7 continuity in mortgage lending as an important field of
8 investment for savings entrusted to them. At a meeting
9 in March the banks agreed to resume operations in this
10 field on much the same scale as in 1956.....Bank of
11 Canada indicated that the total resources of the banks as
12 a group could be expected to increase during 1957 by an
13 amount at least great enough to take care of their
14 disbursements on mortgage loans in that year, so that it
15 would not be necessary for the banks to dispose of other
16 assets in order to maintain a flow of funds for insured
17 housing loans.

18 Exhibit 40. J.E. Coyne - 1956 Report

19 Long term investments made from and limited by
20 funds accruing from the growth of savings deposits are in
21 quite a different category from credit expansion in the
22 form of current or demand loans to businesses and
23 individuals, which may reach excessive proportions....the
24 financing of such credit expansion through the use of
25 funds arising from savings deposits, both directly and from
26 the sale of Government bonds in which savings deposits
27 previously received had been invested, has been one of
28 the less predictable and less stable features of monetary
29 developments over the past two years.....In Canada this
30 has been more noticeable perhaps than elsewhere because of

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financing of such credit expansion through the use of the sale of Government bonds in which savings deposits previously received had been invested, has been one of the less predictable and less stable features of monetary developments over the past two years.... In Canada this has been more noticeable perhaps than elsewhere because of



1 the extent to which commercial banking functions and
2 savings banking functions are intermingled in the
3 operations of the chartered banks. Over 80 per cent of
4 total personal savings deposits in Canada are held with
5 the chartered banks, and the pattern of investment of
6 such deposits has varied widely at different times. The
7 banks may under conditions of inflationary pressure
8 expand their commercial and general loans and other forms
9 of short-term credit from such funds, which in other
10 times would go into long-term investments....the avail-
11 ability for commercial and general loans of funds that
12 can be obtained by the banks by selling in large volume
13 the Government securities in which a considerable pro-
14 portion of their savings deposits had previously been
15 invested. By this means, the greater part of the
16 resources of the banks' savings departments have been
17 available as required from time to time to augment the
18 other resources of the banks' commercial banking
19 departments when the demand for commercial loans has been
20 particularly great.....

21 Exhibit 41. J.E. Coyne - 1959 Report

22 By April the banks were becoming concerned
23 about the rate of growth in their loans. On May 14
24 following a series of meetings the President of the
25 Canadian Bankers' Association issued a public statement
26 saying that the banks intended to exercise the utmost
27 care in the handling of their credit facilities, in order
28 to avoid any significant further increase in the over-
29 all total of bank loans, and that within these limitations,
30 a special attempt would be made to look after the

the extent to which commercial banking functions and savings banking functions are intermingled in the operations of the chartered banks. Over 80 per cent of total personal savings deposits in Canada are held with the chartered banks, and the pattern of investment of such deposits has varied widely at different times. The expansion of their commercial and general loans and other forms of short-term credit from such funds, which in other respects would be their main source of funds that ability for commercial and general loans of funds that can be obtained by the banks by selling in large volume the Government securities in which a considerable proportion of their savings deposits had previously been invested. By this means, the greater part of the resources of the banks' savings departments have been available as required from time to time to augment the other resources of the banks' commercial banking departments when the demand for commercial loans has been particularly great.....

Witness: Mr. J. E. Doyle - 1920

By April the banks were becoming concerned about the rate of growth in their loans. On May 14 following a series of meetings the President of the Canadian Bankers' Association issued a public statement saying that the banks intended to exercise the utmost care in the handling of their credit facilities, in order to avoid any significant further increase in the over-all total of bank loans, and that within these limitations a special attempt would be made to look after the



1 essential credit needs of small borrowers.

2 At the annual meeting of the Canadian Bankers'
3 Association on June 12, 1959, the President in his
4 published address re-affirmed the statement of May 14.

5 Nevertheless, the banks experienced great
6 difficulty in bringing their loans under control.....

7 Exhibit 42. Hon. D.M. Fleming - House of Commons, 1962.

8There has been no change in policy. After
9 Mr. Rasminsky had taken over his duties last summer as
10 governor of the bank he met with representatives of a
11 number of leading investment houses in Canada and proposed
12 to them that for the time being it would be desirable that
13 they should not undertake financing in the United States
14 market, with the opportunities that existed in Canada
15 for that purpose. It was expected that this would be for
16 a temporary period and, in view of the governor, that
17 period has now been concluded. All he did was to inform
18 the financial houses that he would no longer ask them, as
19 I am informed, to refrain from doing financing in the
20 United States market if they thought it proper to do so,
21 but he has not suggested to them that they should do so.

22 Exhibit 43. Macmillan Report

23 235. We are now in a position to sum up our
24 general views on the question of a central banking
25 institution for Canada. We should perhaps sound a note
26 of warning as to the degree to which such an institution
27 could fulfil all the expectations that the public mind
28 might attach to it. A central bank could not cure all
29 the economic ills of Canada; it would not be a source of
30 unlimited credit for all borrowers on all occasions;



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Exhibit #3. Statement of Joseph

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1 indeed its operations might as often be restrictive as
2 expansive.

3 G.F. Towers - House of Commons, 1939.

4 No amount of monetary expansion can hope to
5 restore a high level of real national income in Canada
6 during a period when there is a major decline....in the
7 demand for our goods in foreign markets....it cannot
8 create an important demand for goods which we would
9 normally export nor can it....create new industries to
10 absorb man-power.....from depressed export industries....

11 G.F. Towers - House of Commons, 1954.

12I certainly would not suggest that
13 monetary policy, or indeed the best of fiscal policies,
14 are all that is needed to ensure a prosperous country. I
15 think they can help. But I do not think, the two things
16 can in any way be completely divorced. In other words, I
17 think that they are a team which has to be driven in
18 double harness. A monetary policy which is striving to
19 counteract inflation will be defeated by a fiscal policy
20 which is highly inflationary.....While there could be
21 variation in one or the other, depending upon the general
22 situation, they must be generally non-contradictory.....
23 if you have a country in which the fiscal policy is
24 extremely inflationary, then the central bank cannot
25 prevent the resultant extremes.....

26 J.E. Coyne - 1956 Report

27 It is doubtful if monetary policy can be
28 expected by any reasonable degree of severity in its
29 application to prevent price inflation entirely in the
30 fact of pressures of the nature and degree experienced

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J.E. Coyne - 1950 Report

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1 last year in Canada and in many other countries.....Since
2 it is the duty of the central bank to resist excessive
3 tendencies towards either inflation or deflation in the
4 economy, it has sometimes been described as being required
5 to "lean against the wind". Perhaps a more accurate
6 description would be to say that in seeking to act as a
7 stabilizing factor in relation to the total rate of
8 spending in the economy, the job of the central bank is
9 to yield somewhat to the wind but offer increasing
10 resistance.....While the central bank can influence the
11 quantity of money (currency and bank deposits), there is
12 no fixed relationship between the quantity of money and
13 the rate of spending. At any given moment a varying
14 proportion of the money supply is inactive, lying in
15 dormant deposits, but capable of being activated if
16 sufficient incentive is offered. Rising interest rates
17 and increased efforts by would-be borrowers cause the
18 owners of previously inactive deposits to lend them to
19 those who want to make capital expenditures, or other
20 expenditures.....The maintenance of orderly conditions
21 in financial markets, and the avoidance of a serious
22 disruption of the flow of funds from savings to investment,
23 is a responsibility of a central bank, both in the
24 interests of economic growth and in the interests of
25 government finance and the government securities market
26 through which (by buying or selling securities) the
27 central bank is able to regulate the money supply.

28 J.E. Coyne - 1957 Report

29 There are limits to the role of monetary policy
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1 force to a country so dependent upon foreign trade as
2 Canada. We must view the changing economic conditions
3 in our economy in the context of the vicissitudes of our
4 great trading partners.....Many of the investment decisions
5 with regard to resource development in Canada are made
6 by non-resident investors. Much depends on the degree of
7 business optimism outside our borders as well as within
8 Canada.....But this does not absolve us from the
9 necessity of having a monetary policy of our own, in order
10 to minimize the adverse effects of developments abroad
11 and to inhibit the growth of unfavourable fluctuations
12 of domestic origin.

13 Louis Rasminsky - July 31, 1961, Statement

14 Too much reliance on monetary policy either as
15 a restraining or a stimulating factor would, however, lead
16 to unsatisfactory self-defeating results. If one were
17 to try to control the excesses of a boom period through
18 monetary policy without adequate support from appropriate
19 fiscal, debt management and other economic policies of
20 Government, one would run the risk of creating great
21 strains in the financial system in the form of intolerably
22 high interest rates and disorganization in capital markets.
23 On the other hand, the precise part that monetary policy
24 can appropriately play in stimulating economic expansion
25 is necessarily influenced by the part being played by the
26 concurrent fiscal, debt management and other economic
27 policies of Government. The central bank has an
28 important part to play in influencing the trend of
29 interest rates in a direction appropriate to the economic
30 situation. But an attempt on its part to impose a level



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1 of interest rates which appeared unrealistic to the
2 market would impair confidence in the value of the
3 currency and present a serious obstacle to the orderly
4 flow of funds through the capital market.

5 Louis Rasminsky - 1961 Report

6 Good economic performance depends both on
7 financial policies and on the basic elements of economic
8 efficiency -- a well-trained, energetic and adaptable
9 working population, dynamic business leadership, the
10 imaginative application of modern technology, good
11 marketing practices, and perhaps above all the deter-
12 mination to be competitive. These basic factors need
13 an environment of appropriate financial policies if they
14 are to make their maximum contribution to the achievement
15 of our economic goals. But if the basic factors them-
16 selves are missing, their absence cannot be adequately
17 compensated by variations in the cost and availability of
18 credit, or by variations in the foreign exchange rate, or
19 indeed by any kind of purely financial management.

20 Quest for Stability

21The Federal Rserve is limited in what it
22 can accomplish through influencing the money flow. In
23 the first place, the System can influence only one of the
24 two determinants of the flow of money expenditures --
25 the quantity of money but not its velocity of circulation.
26 Second, the instruments available to the System are more
27 effective in checking a boom than in promoting recovery
28 from a depression. Inflation can be checked by limiting
29 the money supply, but expansion can only be encouraged
30 during depression by making more reserves available. It



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1 is more effective "to pull on a string than to push";
2 nevertheless, by providing banks with an amply supply of
3 reserves and putting a plentiful supply of funds in the
4 market, the System can at least cushion a decline.....If
5 labour and other organized groups exert enough pressure
6 to force money incomes up faster than the increase in
7 productivity, monetary and fiscal authorities may be con-
8 fronted with choosing between two alternatives -- an
9 expansion in the money supply to support higher costs and
10 rising prices, or unemployment. Thus monetary and fiscal
11 policies, no matter how well conceived and expertly
12 executed, may not be able to maintain stability in the
13 face of inappropriate wage and other income policies.

14 W. McC. Martin - 1961 Speech

15 The Federal Reserve intends now, as in the past,
16 to make vigorous use of its monetary powers in order to
17 contribute to the attainment of conditions conducive to
18 a productive, actively employed, steadily growing economy
19 with relatively stable prices.

20 But clearly those conditions cannot be provided
21 by monetary policy alone. Help is needed, especially in
22 directly attacking some of the problems of unemployment
23 that cannot reasonably be solved by credit measures.

24 Without such help, we might find at some point that the
25 plague of unemployment was still with us, but by then it
26 had been compounded by inflation.

27 What is needed, in my judgment, is a judicious
28 blend of specific actions, well-balanced monetary and
29 fiscal policies, and wage-price policies fitting to a
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Neither can we afford to be priced out of the market by currency inflation: in our governmental processes we must guard against reckless budgetary and monetary practices that can undermine the value of our currency, and with it undermine our competitive position as both sellers and buyers of goods and services throughout the world.

Lord Cobbold - 1961

"I also accept -- indeed it is a theme which I have myself argued for many years past -- that monetary policy cannot cure all ills and that it is a great mistake to expect it to carry loads which should be carried in other fields of government policy." As quoted by Honourable Donald M. Fleming in the House of Commons, February 21, 1961.

Exhibit 44. J.E. Coyne -- 1960 Speech

.....In a serious depression, unemployment is of such a magnitude and of such a widespread character that general measures of monetary expansion and deficit financing may be expected to make a major contribution towards encouraging an increase in production and unemployment throughout the country. Of course, no great assistance will be derived by industries dependant upon export markets from an increase in spending and spending power merely within Canada itself. If, however, industries producing for the domestic market are also suffering from serious and general under-employment -- and if this is not due to high costs and inability to compete with imports but is a reflection of a low level of spending within the country -- it is apparent that general



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1 measures to increase the ability of people and businesses
2 to spend, and to undertake new projects with the aid of
3 borrowed money, may have a quite pronounced beneficial
4 effect. Such measures can in such circumstances improve
5 the rate of activity in industries producing for the
6 domestic market, including of course a wide variety of
7 service industries as well as goods-producing industries.

8 On the other hand, what has not been so widely
9 recognized is that if unemployment is not general but
10 is chiefly apparent in the export industries, or is
11 scattered in particular industries or particular
12 localities for reasons peculiar to those industries or
13 localities, a general increase in money and credit, with
14 or without a general degree of deficit spending by
15 the government, will not necessarily have any useful
16 effect on the particular areas of unemployment in
17 question. Moreover, if at such a time industries
18 producing for the domestic market are for the most part
19 operating at a high level -- or even if they are under-
20 employed where the cause is inability to compete with
21 imports -- one would expect that a general expansion of
22 the money supply and of credit available through the
23 banking system, or large scale government deficits, would
24 tend to result in increased imports -- that is to say in
25 a stimulus to production and employment outside Canada --
26 rather than increased production and employment inside
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APPENDIX D

MUNICIPAL FINANCE

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APPENDIX D
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MUNICIPAL FINANCE

INTRODUCTION

1. The division of responsibility among the different levels of government in Canada is most complex. Responsibility for matters primarily affecting only local residents forms the basis for the existence, and the delineation of authority, of the Canadian municipality. Such matters include protection to persons and property, local public works, sanitation, health and welfare, and recreation. While education is considered to be a provincial responsibility, the provision of educational facilities and teachers is treated as a local responsibility, to be supported in part, or entirely, by local resources. In order to carry out these responsibilities the municipality possesses the power to borrow capital funds for the provision of the necessary capital works.

2. However, the Canadian municipality owes its existence and its authority to the province in which it is situated. Consequently, the provinces can and do exercise considerable control over their municipalities and accept substantial responsibility for their welfare. The provinces differ somewhat in their views as to the extent to which provincial authority and responsibility should be exercised, with the result that varying degrees of municipal autonomy and provincial assistance exist across Canada.

3. The municipality's special sphere of operations has created unique financing operations and market characteristics for municipal obligations which make it desirable to consider municipal capital financing

THE CANADIAN FINANCEINTRODUCTION

1. The division of responsibility among the different levels of government in Canada is most complex. Responsibility for public services is divided among the federal government, the provinces, and the municipalities. The basis for the existence, and the delineation of authority, of the Canadian municipality. Such matters include protection to persons and property, local public works, sanitation, health and welfare, and recreation. While education is considered to be a provincial responsibility, the provision of educational facilities and teachers is treated as a local responsibility to be supported in part, or entirely, by local resources. In order to carry out these responsibilities the municipality possesses the power to borrow capital funds for the provision of the necessary capital works.

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3. The municipality's special sphere of operations has created unique financing operations and market characteristics for municipal obligations which make it desirable to consider municipal capital financing



separately from provincial finance. Comment on its various aspects has been divided as follows:

- I Sources of Capital
- II Sale of New Debenture Issues by the Municipality
- III The Evaluation of Municipal Debentures
- IV The Market for Municipal Debentures
- V Marketing Assistance from Senior Governments

I SOURCES OF CAPITAL

4. A municipality has three basic sources of capital, namely: current revenues, grants from senior governments and proceeds from the sale of its debentures. The federal and provincial governments do make capital grants for construction costs of certain works including hospitals, homes for the aged, some roads and bridges, schools, and water and sewer works, but the largest source of capital is the proceeds from the sale of new debentures.

5. The rapid population growth since 1945, as well as the trend to higher standards of municipal services, has resulted in constantly increasing municipal capital requirements. A number of provinces have adopted measures to assist municipalities in borrowing for these capital funds, including the establishment of provincial corporations to buy municipal debentures with funds raised by the sale of the corporations' own provincially guaranteed bonds. Such corporations include the Alberta Municipal Financing Corporation (a) and the Ontario Municipal Improvement Corporation (b). The former

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1 provides all capital funds required by Alberta
2 municipalities at rates in accordance with the cost of
3 money borrowed by the Corporation, plus operating costs.
4 The latter is designed to provide capital only to those
5 municipalities which are not in a position to borrow
6 in the market at reasonable rates.

7 6. In some provinces, part of the capital
8 raised by debenture sales is, in effect, provided by the
9 province by means of annual grants of a percentage of
10 annual service charges on debentures. This procedure
11 helps preserve autonomy and self-reliance, as the
12 municipality or school board still has an interest in
13 striving for low borrowing costs. Such grants do result
14 in lower borrowing costs. This occurs because the
15 percentage of debenture debt supported by grants may be
16 excluded from debt to be paid from taxes. In general,
17 the lower the tax supported debt, the better the credit
18 rating, resulting in lower borrowing costs.

19 (a) The Alberta Municipal Financing

20 Corporation Act, Chapter 3, Statutes
21 of Alberta, 1956.

22 (b) Ontario Municipal Improvement Corporation

23 Act. Chapter 263, Revised Statutes of
24 Ontario, 1950.

25 II SALE OF NEW DEBENTURE
26 ISSUES BY THE MUNICIPALITY

27 7. The traditional method of selling new
28 debenture issues has been to call for tenders from
29 investment dealers. It is reasonable to assume that,
30 under normal market conditions, an established



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(a) The Alberta Municipal Financing Corporation Act, Chapter 14, R.S.A. 1980

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(b) Ontario Municipal Improvement Corporation Act, Chapter 203, Revised Statutes of Ontario, 1980

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II SALE OF NEW DEBENTURES ISSUED BY THE MUNICIPALITY

7. The traditional method of selling new

debenture issues has been to call for tenders from investment dealers. It is reasonable to assume that, under normal market conditions, an established



1 municipality with a moderate capital borrowing programme
2 can achieve the best results by this method.

3 8. However, there are many Canadian
4 municipalities which are not always in such a fortunate
5 position. A municipality with a heavy borrowing
6 programme in prospect for several years may be well
7 advised to market its large issues through a fiscal
8 agency group, thus assuring broad distribution
9 facilities to assist in the successful sale of each
10 issue. Municipalities which have adopted the fiscal
11 agency method include the cities of Ottawa, Hamilton
12 and Vancouver and the Municipality of Metropolitan
13 Toronto.

14 9. A municipality in a special situation, one
15 which needs its story well told, will also benefit from
16 the services of fiscal agents. Such a municipality
17 might have had past difficulties only recently overcome,
18 be newly created, or have changed in character due to
19 annexation or rapid urban development. Municipalities
20 which have sold debentures through fiscal agents for one
21 of these reasons include District of Kitimat, B.C., City
22 of Windsor, Ontario, the County of Halifax, N.S. and the
23 Township of Toronto, Ontario.

24 10. In general, the smaller but well
25 administered municipality can afford to try for the
26 highest possible price on each issue as it comes along,
27 with the knowledge that a poor marketing operation on any
28 one issue is unlikely to affect its general credit
29 rating or its future issues.

30 11. The manner of calling for tenders is

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rating or its future issues.

one issue is unlikely to affect its general credit

with the knowledge that a poor marketing operation on any

highest possible price on each issue as it comes along,

administered municipality can afford to try for the

10. In general, the smaller but well

Township of Toronto, Ontario.

of Windsor, Ontario, the County of Halifax, N.S. and the

of these reasons include District of Kitchener, B.C., City

which have sold debentures through fiscal agents for one

annexation or rapid urban development. Municipalities

be newly created, or have changed in character due to

might have had past difficulties only recently overcome,

the services of fiscal agents. Such a municipality

which needs its story well told, will also benefit from

9. A municipality in a special situation, one

Toronto.

and Vancouver and the Municipality of Metropolitan

agency method include the cities of Ottawa, Hamilton

issue. Municipalities which have adopted the fiscal

facilities to assist in the successful sale of each

against the time when the

advised to market its large issues through a fiscal

programme in prospect for several years may be well

position. A municipality with a heavy borrowing

municipalities which are not always in such a fortunate

8. However, there are many Canadian

can achieve the best results by this method.

municipality with a moderate capital borrowing programme

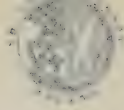


1 worthy of attention. In many instances tender notices
2 are despatched to selected lists of dealers. However, in
3 most cases where notices have appeared publicly, the
4 responses have been more numerous and consequently more
5 indicative of market levels. It is suggested that notices
6 be published in the Official Gazette of the province
7 concerned so that all dealers would have the opportunity
8 to submit tenders. Issues should be awarded to the
9 tenderer whose bid provides capital at the lowest cost,
10 provided that the borrower and provincial authorities are
11 satisfied with the financial stability of the bidder and
12 that the tender is in accordance with the terms and
13 conditions contained in the call for tenders.

14 III THE EVALUATION OF MUNICIPAL DEBENTURES

15 12. The value of a municipal debenture is
16 determined by comparing the features of the issuer with
17 those of other municipal borrowers in order to establish
18 a relative worth. Obviously certain basic information
19 must be obtained before accurate evaluation can be made,
20 and many dealers in municipal debentures have declined
21 to bid for new issues, at one time or another, simply
22 because sufficient information was not made available.

23 13. The items usually considered to be most
24 important are the amount, quality and diversity of
25 assessment, the tax collection record, the weight of debt
26 and the debt history. A more detailed list of relevant
27 items is contained in Exhibit "A:", appended. While the
28 information referred to in this Exhibit is more detailed
29 that is necessary in many instance, a good general rule
30 is that the more information available, the more



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III THE EVALUATION OF MUNICIPAL DEBENTURES

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important are the amount, quality and diversity of assessment, the tax collection record, the weight of debt and the debt history. A more detailed list of relevant items is contained in Exhibit "A", appended. While the information referred to in this Exhibit is more detailed than is necessary in many instances, a good general rule is that the more information available, the more



1 satisfactory the sale of debentures is likely to be.
2 14. It is usually difficult to compare the
3 financial positions of municipalities in different
4 provinces because bases of assessment and municipal
5 accounting procedures vary from province to province, and
6 sometimes from municipality to municipality in the same
7 province. Most provinces publish some form of annual
8 municipal statistics which appear to be standardized for
9 their own municipalities at least. Many of these
10 publications are far from satisfactory, however, as they
11 contain insufficient facts and little information. Steps
12 should be taken to rectify this lack of data.

13 15. Once the basic value of a municipal
14 debenture is established and an approximate market rate
15 arrived at by comparison with other issues, this rate is
16 adjusted for the features of the issue itself. These
17 features include the term to maturity, redemption clause
18 and coupon interest rates.

19 IV THE MARKET FOR MUNICIPAL DEBENTURES

20 16. Canadian and American investing institutions
21 are the largest buyers of Canadian municipal debentures
22 and slightly over sixty per cent of those outstanding are
23 held by this category. The most important Canadian
24 institutional purchasers of the shorter maturities are
25 chartered banks, trust companies and Quebec financial
26 co-operatives (caisses) and of the longer maturities,
27 insurance companies and ~~pension~~ funds.

28 17. The estimated distribution of municipal
29 debenture holdings is given in Exhibit "B", appended. It
30 will be noted that some 35 per cent of the debentures held

satisfactory the sale of debentures is likely to be.
14. It is usually difficult to compare the

financial positions of municipalities in different
provinces because bases of assessment and municipal
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will be noted that some 35 per cent of the debentures held



1 in Canada are owned by investors other than institutional
2 and government accounts.

3 18. The annual capital requirements of Canadian
4 municipalities are substantial, the estimated \$471 million
5 requirements in 1961, representing some 46.5 per cent of
6 total provincial financing. Exhibit "C" shows the dollar
7 volume of new provincial and municipal issues sold in
8 recent years. The dollar volume sold to Canadian
9 institutional buyers has depended to some extent on the
10 yield spread from provincial bonds. While insurance
11 companies do allocate specific amounts of investment
12 funds for the purchase of particular classes of securities,
13 it has been proven many times that such allocations may
14 be adjusted readily when one class appears more or less
15 attractive in yield than others. It will be seen from
16 the exhibit that substantial amounts of capital have
17 been raised in the past through the sale of both
18 provincial and municipal issues outside of Canada. This
19 form of borrowing has been necessitated by the fact that
20 demands on the internal market have been so heavy that
21 it would have been difficult for it to completely absorb
22 the volume of new issues. There has been the added
23 advantage that in most cases external borrowings have
24 been effected at more advantageous rates than were
25 available in Canada at the time. However, the imposition
26 of a 15 per cent Federal Withholding Tax could increase
27 the cost to Canadian borrowers to such an extent as to
28 make external borrowing uneconomical, as foreign
29 investors require an increase in yield in order to
30 compensate them for the loss involved due to the tax.

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 compensate them for the loss involved due to the tax.



1 With the large volume of financing facing our municipal-
2 ities in the foreseeable future, we recommend that the
3 tax be rescinded so that this source of funds will again
4 be available to them.

5 19. The marketing of municipal debentures is
6 more specialized than provincial and many corporate
7 securities. One of the reasons for this is the
8 preponderance of serial forms of issues. Some
9 municipalities have adopted the installment type instead
10 of the true serial. In its original form, a twenty year
11 installment issue, which is based on equal annual
12 installments of principal and interest, comprises twenty
13 different maturities with a varying amount of debentures
14 in each maturity and at least one debenture in each
15 maturity with a par value of an odd number of dollars
16 and cents. The maturities comprising an actual debenture
17 issue which was marketed in 1960 are shown in Exhibit
18 "D". It is difficult to sell serial issues to the
19 general public because of the problems in merchandising
20 so many different maturities, frequently at different
21 dollar prices. Many investors dislike the bookkeeping
22 and handling problems involved in a multi-maturity
23 investment.

24 20. Institutional investors and private
25 individuals form the two groups that purchase municipal
26 and school debentures. The former may be divided into
27 two categories, the chartered banks, trust companies and
28 Quebec financial co-operatives forming one and insurance
29 companies, pension funds and various government accounts
30 the other. The first category usually prefers short term



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ities in the foreseeable future, we recommend that the
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general public because of the problems in merchandising
so many different issues, and the fact that the
maturities are so small and the interest rates are low.
and handling problems involved in a multi-maturity

20. Traditional investors and private
individuals form the two groups that purchase municipal
and school debentures. The former may be divided into
two categories, the chartered banks, trust companies and
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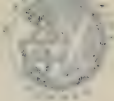


1 serials maturing not later than ten years, although there
2 are times when they may stop at earlier maturities. On
3 the other hand while insurance companies and pension
4 funds may prefer long term non-callable sinking fund
5 debentures, they do buy long term serials. The require-
6 ments of individuals vary from person to person. This
7 leads us to believe that issues containing serial
8 maturities in the early years as well as a long term
9 sinking fund maturity or maturities should satisfy the
10 requirements of the various types of investors. In
11 following this method, it should be possible to vary the
12 maturity dates of the serial and sinking fund debentures
13 in accordance with changing market conditions.

14 21. It is usually difficult to maintain active
15 secondary markets for debentures of smaller borrowers.
16 The operations of sinking funds would certainly create
17 some demand for the outstanding debentures of these
18 borrowers.

19 It will be helpful if sinking funds which are
20 established against specific issues are not restricted to
21 the purchases of debentures of those same issues but
22 would be open to any debentures of the borrower. With the
23 exception of larger municipalities, sinking funds should
24 be supervised by the appropriate provincial authorities
25 in order to provide knowledgeable assistance.

26 22. There are two federal requirements at
27 present which tend to restrict the market for municipal
28 and school board debentures to some extent. For the
29 purpose of annual portfolio evaluation by Canadian Life
30 insurance companies, the Department of Insurance allows



are times when they may step at earlier maturities. On the other hand while insurance companies and pension funds may prefer long term non-callable sinking fund debentures, they do buy long term serials. The requirements of individuals vary from person to person. This leads us to believe that issues containing serial maturities in the early years as well as a long term maturity would be desirable. In following this method, it should be possible to vary the maturity dates of the serial and sinking fund debentures in accordance with changing market conditions.

21. It is usually difficult to maintain active secondary markets for debentures of smaller borrowers. The operations of sinking funds would certainly create some demand for the outstanding debentures of these borrowers. It will be helpful if sinking funds which are established against specific issues are not restricted to the purchases of debentures of those same issues but would be open to any debentures of the borrower. With the exception of larger municipalities, sinking funds should be supervised by the appropriate provincial authorities in order to provide knowledgeable assistance.

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1 the evaluation of federal and provincial obligations,
2 both direct and guaranteed, to be the companies' amortized
3 book values. However, this method is not accepted for
4 municipal securities. This tends to make such obligations
5 relatively more attractive than municipal obligations to
6 life insurance companies than would otherwise be the
7 case. Consideration should be given to allowing
8 insurance companies to evaluate municipal debentures in
9 a like manner.

10 23. The Department of Insurance in Ottawa
11 requires non-resident insurance companies to deposit,
12 with it, acceptable bonds and debentures as security for
13 these companies' Canadian policy holders. Municipal
14 debentures are acceptable for this purpose but school
15 debentures are not eligible for deposit unless they
16 bear a provincial or municipal guarantee. The acceptance
17 of school debentures for deposit would benefit the market
18 for these securities.

19 24. There is a strong feeling among many
20 municipal officials that the issuance of tax-exempt
21 debentures in Canada, similar to those issued by United
22 States borrowers, would result in substantially lower
23 debt service charges to Canadian issuers. At first glance
24 this appears to be the case, but further study proves it
25 to be doubtful. For instance pension funds, large buyers
26 of municipal securities, would derive no benefit whatever
27 from the exemption so that they would be lost to the
28 market. Taxation of chartered banks and insurance
29 companies is not based solely on investment income, so
30 that the exemption might have little appeal to them and



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1 their purchases could decrease. This would result in
2 upper bracket taxable accounts being the principal source
3 of capital available to municipalities and the volume that
4 might be generated from this source might not be
5 substantial. It is possible that a few tax-exempt issues
6 might be successfully sold, but it would not take long
7 for the yields on tax-exempts to increase so as to almost
8 coincide with those on taxable securities. For these
9 reasons we recommend that tax-exempt status not be given
10 to municipal debentures. Recent experience in the United
11 States tends to support this conclusion as is indicated
12 by the appended quotation from an article "Should the
13 Income Tax be Overhauled?" in the December 1961 Monthly
14 Review, issued by The Federal Reserve Bank of Kansas
15 City (Exhibit "E").

16 V MARKETING ASSISTANCE BY PROVINCIAL
17 GOVERNMENTS

18 25. The various provinces assist their
19 municipalities in one way or another to sell debentures.
20 The simplest form of assistance, one which has proven
21 very effective, is to require municipalities to provide
22 information about their history, economic and financial
23 condition, and details of the proposed issues. The
24 information is included in standard information forms
25 which are made available to prospective bidders. In some
26 instances the provinces issue calls for tenders incorp-
27 orating this information.

28 26. Another effective device is being used by
29 some of the provinces in assisting in the marketing of
30 school debentures. These provinces remit agreed upon



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1 grants to the paying agents for the debentures with the
2 proviso that the funds are to be used in the servicing of
3 the debt in the years in which the grants are received.
4 This improvement in the security of school debentures
5 has resulted in borrowing costs being substantially lower
6 than otherwise would have been the case. However, we
7 recommend when grants are not statutory that they be made
8 so rather than continuing the present practice of
9 requisitioning the amounts annually. In addition to
10 this their description in the texts of the debentures
11 secured by them should assist in a wider acceptance of
12 this type of investment.

13 27. In some provinces assistance has been
14 offered to the underwriter, rather than directly to the
15 municipality, by purchases by provincial accounts of
16 some part of each issue. In some cases the purchasing
17 intentions of these accounts are made known to dealers
18 prior to the sale of the debentures. In other instances
19 the province has made known its policy of assistance by
20 government account purchases in the event that the issue
21 is not successfully marketed within a reasonable time.
22 This policy has had the double effect of increasing
23 dealer confidence in underwriting municipal issues and
24 of avoiding the adverse effects that unsold issues have on
25 the new issues of adjacent and similar municipalities.

26 28. Probably the most effective form of
27 provincial marketing assistance has been the provincial
28 guarantee of principal and interest payments. All
29 provinces have resorted to this device at one time or
30 another and it is undoubtedly of major assistance in



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marketing issues of little know or low rated
municipalities and school-boards.

MUNICIPAL FINANCE, RECOMMENDATIONS FOR
THE I.D.A.C. BRIEF

- Pr. 22 a) We recommend that life insurance companies
Page 7 be permitted to evaluate their holdings
of municipal securities at the amortized
book values following the same practice as
for federal and provincial obligations.
- Pr. 23 b) We recommend that the Federal Department
page 7 of Insurance accept school debentures for
deposit by non-resident insurance companies.
- Pr. 24, c) We recommend that the tax status of
page 8 interest payments on municipal debentures
Exhibit "E" remain unchanged.

---O---



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municipalities and school-boards.

MUNICIPAL FINANCE, RECOMMENDATIONS FOR
THE 1939-40 YEAR

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for federal and provincial obligations.

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of Insurance accept school debentures for

deposit by non-resident insurance companies.

Pr. 24 c) We recommend that the tax status of

interest payments on municipal debentures

remain unchanged.



EXHIBIT "A"

Evaluation of Municipal Debentures

Factors Affecting a Municipality's Credit Rating

General

1. Geographical location
2. Physical appearance, size (acreage)
3. Economy - a) type - agricultural, industrial etc.
- b) extent and wealth of marketing area
- c) quality of housing
4. Condition and extent of municipal facilities
- a) water service
- b) sewer service and treatment
- c) roads, sidewalks, bridges
5. Extent of control over development
- a) zoning by law
- b) in rural or semi-rural, method of controlling urban growth
6. Management
- ability of council and political climate
- ability of appointed officers

Statistical Statistics for at least the past five years are examined so that trends may be detected.

7. Population

- a) total
- b) rate payers

8. Assessment

- a) residential, commercial and industrial categories
- b) per capita



ANNEX A

Evaluation of Municipal Performance
Factors Affecting a Municipality's Credit Rating

General

1. Statistical Information
2. Physical appearance, size (acres)
3. Economy - a) type - agricultural, industrial etc.
- b) extent and weight of marketing
- c) quality of housing
4. Condition and extent of municipal facilities
 - a) water service
 - b) sewer service and treatment
 - c) roads, sidewalks, bridges
5. Extent of control over development
 - a) zoning by law
 - b) in rural or semi-rural, method of controlling urban growth
6. Administrative
- ability of council and political climate
- ability of appointed officers

Statistical

Statistics for at least the past five years are examined so that trends may be detected.

Finances

- a) total
- b) rate payers
- a) residential, commercial and industrial categories
- b) per capita



Exhibit "A" - continued

- c) relationship to current market values
- d) exemptions

9. Current Operations

- a) accuracy of budgeting as evidenced by annual surpluses or deficits and outstanding temporary loans
- b) ability of taxpayers to pay and the municipality to collect taxes as shown by current and total tax collections as a percentage of current levy and total outstanding tax arrears as a percentage of current levy and per capita. Explanation of arrears, if unduly high, such as date tax bills are sent out.
- c) reserves against tax arrears and breakdown of arrears into years in which they occurred.

10. Debt

- a) breakdown: self-supporting
 - local improvements
 - general service debt
- b) ability to pay off debenture debt as indicated by the relationship of debt repayable from taxation to population and assessment and by the percentage that annual debt charges are of annual current revenues.
- c) willingness to pay as indicated by debt history.
- d) forecast of future borrowing.

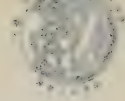


Exhibit "A" - continued

c) relationship to current market values

d) exemptions

Current Operations

a) accuracy of budgeting as evidenced by annual surpluses or deficits and outstanding temporary loans

b) ability of taxpayers to pay and the municipality to collect taxes as shown by current and total tax collections as a percentage of current levy and total outstanding tax arrears as a percentage of current levy and per capita. Explanation of arrears, if unduly high, such as late tax bills are sent out.

c) reserves against tax arrears and breakdown of arrears into years in which they occurred.

Debt

a) breakdown: self-supporting

Long Term Debt

General Obligation Debt

b) ability to pay off debt service as indicated by the relationship of debt repayable from taxation to population and assessment and by the percentage that annual debt charges are of annual current revenues.

c) willingness to pay as indicated by debt history.

d) forecast of future borrowing.



EXHIBIT "B"

ESTIMATED DISTRIBUTION OF HOLDINGS
OF
MUNICIPAL DIRECT & GUARANTEED DEBENTURES

(Source: Bank of
Canada Statistical
Summary, January 1962).

As at December 31, in \$ millions

1960(1)

1959

1958

1957

1956

Life Insurance Companies (2)	427	456	507	547
Provincial Governments (3)	192	237	257	286
Pension Plans	170	183	205	235
Chartered Banks	168	195	204	208
Municipal Governments (4)	137	158	191	207
Other Insurance Companies (5)	97	103	110	121
Trust & Mortgage Loan Companies (6)	47	55	55	71
Quebec Savings Banks	52	53	47	41
All other residents (residual)	764	819	883	955

TOTAL RESIDENT HOLDINGS

1,877

2,054

2,459

2,671

Non-Resident Holdings

656

780

912

1,024

TOTAL

2,427

2,710

3,371

3,695

Notes:

(1) Estimated

(2) Registered under Federal Insurance Acts

(3) Includes holdings of various Funds under provincial jurisdiction such as hydro commission, workmen's compensation boards, sinking Funds, teachers and civil service pension and superannuation Funds.

(4) Based on a sample of those large cities which provide details of their investments in their published annual reports. Includes holdings of various funds under municipal jurisdiction such as sinking Funds and pension Funds.

(5) Fire and casualty insurance companies and fraternal benefit societies registered under Federal Insurance

(6) Holdings of all such companies registered with the Government of Canada of the Province of Ontario, Acts.

or Quebec, plus holdings of Investors Syndicate of Canada Limited

(incorporated in Manitoba).



(Source: Bank of
Country: Guatemala
Country: Guatemala 1988)

ESTIMATED DISTRIBUTION OF HOLDINGS

REPRODUCED FROM THE ORIGINAL

1920 (7)

As of December 31, 1958 8501
in \$ millions 1959 1958

FILE
100
EFS
151
17
14
EER
172.5
150.4

613
 20
 48
 132
 132
 128
 124
 300

$$\begin{array}{r} 1878.1 \\ 225 \\ \hline 4200.5 \end{array}$$

220
220

TOTAL FREIGHT HOLDINGS

benefits (1) : actor

[illegible]

2

(incorporated in Washington)

100-374141
(Source: Bank of
INDIA)

	RESTRICTED DISTRIBUTION OF HOLDINGS	
10		10
11		11
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Nethercut & Young
Toronto, Ontario

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EXHIBIT "C"
GROSS NEW ISSUES, RETIREMENTS AND NET NEW ISSUES
of
MUNICIPAL DIRECT AND GUARANTEED BONDS (1)

Calendar Year	Gross New Issues Delivered			Retirements (2)			Net New Issues		
	Cdn.\$ Only	Other Currencies	Total	Cdn.\$ Only	Other Currencies	Total	Cdn.\$ Only	Other Currencies	Total
1954	305	38	343	83	20	103	222	18	240
1955	302	42	344	86	25	111	217	17	234
1956	247	108	355	107	24	131	140	84	224
1957	292	123	414	110	26	136	181	97	278
1958	347	148	495	139	33	172	208	115	323
1959	370	146	516	157	33	191	213	113	326
1960	411	122	533	177	38	214	234	85	319
1961	445	29	474	180	41	221	265	(12)	252

NOTES: (1) Excluding Municipal issues guaranteed by provinces, and issues sold directly to provinces.
(2) Excluding Payments into sinking funds.

Source: Bank of Canada Statistical Summary, February 1962.

TO
THE
UNITED STATES OF AMERICA

\$1,063,732.52
CITY OF CORNWALL
6% and 6½% Instalment Debentures

Schedule of Maturities

Year	\$12,000.00 Garage #1,017 Dated: Oct. 1/60 6%	\$75,000.00 Land and Buildings #1,041 Dated: Oct. 1/60 6%	\$86,125.53 Waterworks #1,016 Dated: Oct. 1/60 6%	\$306,412.60 Local Improvements #1,037 Dated: Oct. 1/60 6%	\$102,797.22 Public Sch. Board #1,014 Dated: Sept. 1/60 6%	\$126,059.56 Waterworks #1,015 Dated: Oct. 1/60 6%	\$150,000.00 Cornwall Gen. Hospital #1,042 Dated: Oct. 1/60 6%	\$161,259.35 Filtration Plant #949 Dated: June 1/60 6%	\$2,510.60 Local Improvements #943 Dated: June 1/60 6½%	\$3,744.47 Local Improvements #942 Dated: June 1/60 6½%	\$37,823.19 Local Improvements #941 Dated: June 1/60 6½%
1961	\$2,128.76	\$5,690.10	\$6,534.17	\$23,246.91	\$2,794.50	\$3,426.88	\$4,077.68	\$4,383.77	\$186.05	\$277.48	\$2,802.83
1962	2,256.48	6,031.50	6,926.22	24,641.71	2,962.17	3,632.49	4,322.34	4,646.79	198.14	295.52	2,985.06
1963	2,391.87	6,393.39	7,341.79	26,120.22	3,139.90	3,850.44	4,581.69	4,925.60	211.02	314.73	3,179.09
1964	2,535.38	6,777.00	7,782.30	27,687.43	3,328.29	4,081.47	4,856.59	5,221.14	224.74	335.19	3,385.73
1965	2,687.51	7,183.62	8,249.24	29,348.68	3,527.99	4,326.35	5,147.99	5,534.40	239.34	356.97	3,605.81
1966		7,614.63	8,744.19	31,109.60	3,739.67	4,585.93	5,456.87	5,866.47	254.90	350.18	3,840.18
1967		8,071.51	9,268.84	32,976.16	3,964.05	4,861.09	5,784.28	6,218.46	271.47	404.89	4,089.80
1968		8,555.80	9,824.97	34,954.73	4,201.89	5,152.76	6,131.33	6,591.56	289.12	431.20	4,355.63
1969		9,069.15	10,414.47	37,052.02	4,454.00	5,461.92	6,499.21	6,987.06	307.90	459.23	4,638.75
1970		9,613.30	11,039.34	39,275.14	4,721.24	5,789.64	6,889.16	7,406.28	327.92	489.08	4,940.26
1971					5,004.52	6,137.02	7,302.51	7,850.65			
1972					5,304.79	6,505.24	7,740.66	8,321.69			
1973					5,623.08	6,895.55	8,205.10	8,820.99			
1974					5,960.46	7,309.28	8,697.41	9,350.25			
1975					6,318.09	7,747.84	9,219.25	9,911.27			
1976					6,697.18	8,212.71	9,772.41	10,505.94			
1977					7,099.01	8,705.47	10,358.75	11,136.30			
1978					7,524.94	9,227.80	10,980.27	11,804.48			
1979					7,976.43	9,781.47	11,639.08	12,512.74			
1980					8,455.02	10,368.21	12,337.42	13,263.51			
	\$12,000.00	\$75,000.00	\$86,125.53	\$306,412.60	\$102,797.22	\$126,059.56	\$150,000.00	\$161,259.35	\$2,510.60	\$3,744.47	\$37,823.19

OFFICE OF THE COMMISSIONER

CELL OF COUNTY

... 1911 ...

2017-2018



FEDERAL RESERVE BANK OF KANSAS CITY

MONTHLY REVIEW

December 1961

Should the Income Tax be Overhauled?

Taxing State and Local Interest

A clear-cut example of the economic effects of favoured tax status is found in the market for state and local securities. Because interest paid on these securities is exempt from the Federal income tax, investors are willing to buy state and local bonds as lower yields than those available on other securities..... The preference of investors for tax-exempt bonds has made it possible for state and local governments to borrow at rates substantially below rates paid by other borrowers. However, as state and local government borrowing has mushroomed over the postwar period, the demand of high bracket taxpayers for tax-exempt securities has tended to become satiated. It has thus become increasingly necessary for nontaxable bonds to carry yields that make them appealing to investors in lower tax brackets. In consequence, the rate advantage for state and local issues has diminished considerably in recent years, while the advantage of investing in tax-exempt issues has been enhanced for people in higher tax brackets.

In 1946, tax-exempt issues rated Aaa sold at yields less than one half as high as those on corporate securities of comparable quality. The subsequent heavy volume of municipal offerings has progressively reduced this differential. Last year, for example, Aaa-

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1 rated state and local issues sold at rates nearly three
2 fourths as high as those on comparable corporate issues.
3 It was thus possible for investors in the highest
4 brackets to find substantial shelter from tax progression.
5 A taxpayer in the highest (91 per cent) bracket could
6 realize a tax-free return of \$32,600 per year on a \$1
7 million investment in Aaa-rated state and local bonds
8 at the average rate available in 1960. He could earn,
9 after tax, only about \$4,000 annually from an equal
10 investment in Aaa-rated corporate issues at the average
11 rate for 1960.

12 Not only does this state of affairs provide an
13 unwarranted haven from tax progression, it is often
14 argued, but it also encourages investment in rather
15 safe securities by those who are in the best position to
16 finance riskier private undertakings, the income from
17 which is taxable.

18 Tax exemptions of state and local interest
19 payments has often been defended on the ground that it
20 subsidizes desirable spending programs by reducing the
21 borrowing costs of lower levels of government. However,
22 the postwar decline of the differential between tax-
23 exempt bonds and taxable issues has called into serious
24 question the efficiency of the tax exemption feature as
25 a subsidy for state and local borrowing. Taxpayers in
26 high brackets save in taxes (and the Federal Government
27 thereby loses in revenue) an amount far in excess of
28 the saving of interest costs to lower levels of government.
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thereby loses in revenue) an amount far in excess of the saving of interest costs to lower levels of government



APPENDIX "E"

Part I - Corporation Finance

Part II - Legislation.

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CORPORATION FINANCE

1. A discussion of corporation finance should logically begin with an examination of companies themselves -- how they have grown, how much money has been used in the expansion of corporate enterprise and how this expansion has been financed. It is unfortunate that no one set of figures exists that permits a definitive analysis of changes in the structure of Canadian corporate finance. There are, however, statistics published by various authorities from which conclusions can be drawn that in general are probably fairly accurate.

2. The most comprehensive of these are the taxation data published by the Department of National Revenue, the latest of which relate to the year 1959. During the ten years 1949-59 the number of fully tabulated companies in Canada rose from 35,706 to 86,996; their assets, net of depreciation and depletion writeoffs, grew threefold from \$21 billion to \$63 billion. The following is a summary of the source and application of funds of Canadian business over this ten year period, as derived from the Taxation Statistics.

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TABLE I

Source and Application of Funds of Canadian
Business 1949-59

<u>Application</u>	(S billions)
Increase in net working capital	10.0
Increase in gross fixed assets	23.4
Net investment in subsidiaries and affiliates	7.5
Increase in other assets	2.2
Total applications	<u>43.1</u>

Sources

Depreciation, depletion, etc.	8.7
Retained earnings and other surplus	<u>11.3</u>
Total internal sources	20.0
Other liabilities	6.8
Debt	7.8
Equity (preferred and common stock)	<u>8.5</u>
	<u>43.1</u>

"Other liabilities" include loans due to affiliated companies, liability reserves (including deferred taxes) and deferred income.

3. Four important reservations apply to these figures:

1) The increase in fixed assets and in depreciation is after sales of fixed assets, for which figures are not published. Other data published in the taxation statistics show total capital expenditures by tabulated companies from 1950-59 as \$26.4 billions. Capital cost allowances claimed for tax



Source and Application of Funds of Canadian
Business 1950-59

Application	(\$ billions)
Increase in net working capital	10.0
Increase in gross fixed assets	23.4
Net investment in subsidiaries and affiliates	1.0
Increase in other assets	2.2
Total applications	46.6

Depreciation, depletion, etc.	8.7
Retained earnings and other surpluses	11.3
Total internal sources	20.0
Other liabilities	6.8
Debt	7.8
Equity (preferred and common stock)	8.5

"Other liabilities" include loans due to affiliated

and deferred income.

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- 1) The increase in fixed assets and in depreciation is after sales of fixed assets, for which figures are not published. Other data published in the taxation statistics show total capital expenditures by consolidated companies from 1950-59 as \$26.4 billions. Capital cost allowances claimed for tax



1 purposes amounted to \$14.8 billions, or
2 56.2 per cent of this amount while retained
3 earnings were a further \$7.6 billions, or
4 28.3 per cent. Cash dividends paid added
5 up to \$10.5 billions out of net profits of
6 \$18 billions, an average pay-out of 60 per
7 cent.

8 2) The increase in surplus includes capital
9 surplus, part of which would consist of
10 proceeds from sale of stock in excess of
11 par value.

12 3) The increase in common and preferred
13 stock would include capitalization of
14 earnings by way of stock dividends.

15 4) There is a certain amount of "double
16 counting" because of the inclusion of all
17 holding companies and their subsidiaries.
18 For example, the full balance sheet of
19 Aluminum Ltd. is included as well as the
20 full balance sheet of the Aluminum Company
21 of Canada. The "net investment in
22 subsidiaries and affiliates" of \$7.5 billion
23 can be related to the increase in "other
24 liabilities" of \$6.8 billion and the rise
25 in equity of \$8.5 billion.

26 5) The companies include wholly owned
27 subsidiaries of foreign concerns, whose
28 financial requirements have, in large
29 measure, been supplied by non-residents.
30 The pattern of financing may well differ

purposes amounted to \$14.8 billion, or
 56.2 per cent of this amount while retained
 58.2 per cent. Cash dividends paid added
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 financial requirements have, in large
 measure, been supplied by non-residents.
 The pattern of financing may well differ



1 from that of domestic companies.

2 4. Subject to these qualifications the table
3 indicates that 38 per cent of the total application
4 of funds was derived from the issuance of long-term
5 debt and equity securities, this proportion being fairly
6 evenly divided between the two.

7 5. A further qualification, however, is that
8 arising from changes in the relative importance of
9 certain types of business. For example, the group
10 comprising finance, insurance and real estate (which
11 does not include the chartered banks and insurance
12 companies as these are not tabulated) has grown at an
13 above average rate and in 1959 possessed approximately a
14 quarter of the total assets of all fully tabulated
15 companies. This group accounted for half of the net
16 investment in subsidiary and affiliated companies over
17 the ten year period, for 42 per cent of the increase in
18 net working capital and 37 per cent of the increase in
19 debt. Debt represents a higher proportion of
20 capitalization for these companies than for business in
21 general. This applies also to utilities, for which there
22 has been a considerable amount of debt financing in the
23 past five years, partly in connection with the
24 establishment of new natural gas transmission and
25 distribution companies.

26 6. It is therefore informative to look
27 briefly at that important and reasonably consistent
28 group of companies engaged primarily in manufacturing.
29 Here, of the total applications of \$14.1 billion over
30 the period 1949-59, 60 per cent was derived from



4. Subject to these qualifications the table

indicates that 58 per cent of the total application of funds was derived from the issuance of long-term debt and equity securities, this proportion being fairly evenly divided between the two.

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existing from changes in the relative importance of certain types of business. For example, the group comprising finance, insurance and real estate (which does not include the chartered banks and insurance companies as these are not tabulated) has grown at an above average rate and in 1959 possessed approximately a quarter of the total assets of all fully tabulated companies. This group accounted for half of the net investment in subsidiary and affiliated companies over the ten year period, for 42 per cent of the increase in net working capital and 37 per cent of the increase in debt. Debt represents a higher proportion of

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6. It is therefore instructive to look

briefly at that important and necessarily constant group of companies engaged primarily in manufacturing. Here, of the total applications of \$14.1 billion over the period 1949-59, 66 per cent was derived from



internally generated funds, 13.5 per cent from "other liabilities", 12 per cent from the issuance of debt and 14.5 per cent from common and preferred stock.

TABLE IIApplication (\$ billions)

Increase in net working capital 2.9

Increase in gross fixed assets 9.1

Net investment in subsidiaries and affiliates 1.9

Increase in other assets .2

Total applications 14.1

Sources

Depreciation, depletion, etc. 4.1

Retained earnings and other surplus 4.3

Total internal sources 8.4

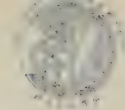
Other liabilities 1.9

Debt 1.7

Equity (preferred and common stock) 2.1

14.1

7. From the more detailed data published on manufacturing in the Taxation Statistics it is interesting to note that capital expenditures over the ten year period amounted to \$11 billion - nearly \$2 billion more than the net increase in fixed assets as shown in the balance sheets - while capital cost allowances claimed for tax purposes totalled \$6.7 billion - \$2.6 billion more than the increase in depreciation reserves shown in the balance sheets. In effect, capital cost allowances were equivalent to 60 per cent of capital outlays during the



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TABLE 10

Application	(\$ billions)
Increase in net working capital	2.9
Increase in gross fixed assets	9.1
Net investment in subsidiaries and	
other assets	
Increase in other assets	
Total applications	14.1
<hr/>	
Retained earnings and other surplus	4.3
Total internal sources	8.4
<hr/>	
Equity (preferred and common stock)	2.1

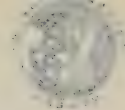
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period.

8. Reflecting the important contribution of internally generated funds, there has been very little weakening in the financial structure of manufacturing companies over the period under review. The working capital ratio, which was 3 in 1949, was 2.75 in 1959; net tangible assets were 8.5 times debt compared with 6 times in 1959; and debt constituted 12 per cent of capitalization as against 17 per cent.

9. Nevertheless, the trend towards a higher proportion of debt in the structure of capitalization is apparent. The reasons, too, are obvious. In some cases, particularly with smaller companies, there is a desire not to dilute ownership of the company. The leverage benefits to common shareholders when earnings are on a generally rising trend, and when return on investment is greater than the cost of servicing debt, favour the issuance of debt within the limits imposed by financial soundness. There are generally accepted rules of thumb in the financial community, developed through experience and which are usually incorporated as covenants in trust deeds, that set these limits. They naturally vary from industry to industry, but in general it can be said that for manufacturing companies it is not considered desirable for debt to represent more than 40 per cent of total capitalization, while for utilities the proportion should not generally exceed 60 per cent (although in certain special cases it could with safety be higher). Similarly interest charges in most cases should be covered at least 3 to 5 times by earnings after



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1 depreciation, but for utilities, because of the greater
2 stability of earnings, a 2 to $2\frac{1}{2}$ times coverage may be
3 sufficient.

4 10. Aside from the factor of leverage there is
5 the further element of cost. Since interest payments may
6 be deducted from corporate income for tax purposes,
7 whereas dividends are not, the cost of issuing debt has
8 been noticeably lower throughout the postwar period
9 than the cost of raising funds through the issue of
10 preferred or common stock. The higher the rate of
11 corporate income tax, the greater is the cost different-
12 ial. In the late 1920's, for example, taxes amounted
13 to only 10 per cent or less of corporate profits, and
14 with the difference between bond and stock yields at
15 that time it was cheaper to issue common stock (although
16 this did not prevent extensive debt financing). Today
17 the tax rate is 50 per cent to 53 per cent, and a
18 company can afford to pay interest at the rate of 8 per
19 cent before the net cost exceeds a dividend rate on
20 shares of 4 per cent. Should the tax rate fall to 40
21 per cent, then an interest rate of 6.7 per cent would be
22 equivalent to a dividend rate of 4 per cent. It would
23 be easier to justify the issuance of stock under such
24 conditions.

25 11. There has been a pronounced tendency over
26 the years for the corporate income tax rate to creep
27 upward. The ramifications of this are many and varied,
28 but the incentive it provides for unsound corporate
29 financing is one which, we feel, should be carefully
30 considered. It would obviously be impractical to suggest

depreciation, but for utilities, because of the greater stability of earnings, a 2 to 2½ times coverage may be justified.

10. Aside from the factor of leverage there is the further element of cost. Since interest payments may be deducted from corporate income for tax purposes, whereas dividends are not, the cost of issuing debt has been noticeably lower throughout the postwar period than the cost of raising funds through the issue of preferred or common stock. The higher the rate of corporate income tax, the greater is the cost differential. In the late 1920's, for example, taxes amounted to only 10 per cent or less of corporate profits, and with the difference between bond and stock yields at that time it was cheaper to issue common stock (although this did not prevent extensive debt financing). Today the tax rate is 50 per cent to 53 per cent, and a company can afford to pay interest at the rate of 8 per cent before the net cost exceeds a dividend rate on shares of 4 per cent. Should the tax rate fall to 40 per cent, then an interest rate of 6.7 per cent would be equivalent to a dividend rate of 4 per cent. It would be easier to justify the issuance of stock under such conditions.

11. There has been a pronounced tendency over the years for the corporate income tax rate to creep upward. The ramifications of this are many and varied, but the incentive is strong for companies to consider financing is one which, we feel, should be carefully considered. It would obviously be impractical to suggest



1 reducing the corporate tax without at the same time
2 pointing out other areas where increased tax revenues
3 might be obtained or expenditures reduced. This could
4 only be done in a comprehensive analysis of the
5 situation of Canadian taxation. We understand that
6 Queen's University is engaged in a study of this nature
7 at the present time.

8 12. It is not surprising to find considerable
9 difference in financial structure according to the size
10 of companies. As shown by the following table constructed
11 from the Taxation Statistics for the year 1959, smaller
12 firms have relatively more recourse to bank financing
13 than the larger; debt constitutes a smaller proportion
14 of capitalization (and much of the debt is represented
15 by mortgages); stock is of much greater importance; and
16 a higher proportion of net profit is retained. These
17 differences reflect the greater ease with which larger,
18 mature companies with long established records of
19 earnings can obtain funds, particularly debt funds, in
20 the market. To some extent they may also reflect the
21 different industries typical of the various asset
22 sizes.



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TABLE III

Financial Structure of Manufacturing Companies by Size of Total Assets - 1959

Companies with Assets	Total Assets (\$ billions)	Working Capital Ratio	% Composition of Capitalization			Surplus	Total
			Debt	Preferred	Common Stk.		
Less than \$100,000	236.6	1.26	6.5%	21.9%	48.0%	23.6%	100%
100 - 250,000	544.4	1.49	8.7	17.2	23.3	50.8	100%
250 - 500,000	622.5	1.61	7.4	16.4	20.9	55.3	100%
500 - 1,000,000	859.5	1.72	6.3	10.1	21.6	61.9	100%
1- 5,000,000	2,499.2	2.22	9.8	10.5	18.7	61.0	100%
5- 10,000,000	1,453.5	2.61	10.00	6.4	22.3	61.3	100%
10- 25,000,000	2,140.9	2.96	15.9	7.8	22.6	53.6	100%
25- 100,000,000	4,763.9	2.76	16.1	6.1	26.1	51.7	100%
100,000,000 - over	7,000.1	2.35	22.3	3.9	26.2	47.6	100%



1917

1917

100,000,000 - 0000	1,000.0	5.32	55.3	3.2	50.5	21.4	100%
50- 100,000,000	4,123.2	27.5	10.1	0.3	50.1	21.4	100%
10- 50,000,000	5,140.5	20.5	12.2	8.7	55.2	23.2	100%
2- 10,000,000	1,123.1	5.21	10.00	4.2	55.3	21.3	100%
1- 2,000,000	5,120.5	5.55	2.8	10.2	12.1	21.0	100%
200 - 1,000,000	2,222	1.15	0.3	10.1	51.2	21.2	100%
50 - 200,000	2,552	1.21	4.7	10.2	50.2	22.3	100%
100 - 50,000	4,142	1.41	2.8	11.5	53.3	20.8	100%
Total from \$100,000	532.2	1.52	0.2	51.5	48.2	53.2	100%

100,000,000 - 0000
50- 100,000,000
10- 50,000,000
2- 10,000,000
1- 2,000,000
200 - 1,000,000
50 - 200,000
100 - 50,000
Total from \$100,000

UNIVERSITY OF MINNESOTA - THE UNIVERSITY OF MINNESOTA - 1917

TABLE III

100,000,000 - 0000
50- 100,000,000
10- 50,000,000
2- 10,000,000
1- 2,000,000
200 - 1,000,000
50 - 200,000
100 - 50,000
Total from \$100,000



BANK OF CANADA DATA

13. The Taxation Statistics apply to all tabulated companies, whether they are privately owned or public, whether they are wholly-owned subsidiaries of foreign parents, or only partially controlled, and whether they are subsidiaries of Canadian firms or independent. The degree to which they have issued debt, preferred stock or common stock does not therefore necessarily bear any relation to the size or composition of security issues in the capital markets.

14. The Bank of Canada, however, publishes data on net new issues of securities by Canadian companies, including banks. These show that from 1949 to 1960 inclusive \$8.8 billion was raised from the issuance of securities, broken down as follows:

Debt \$5.2 billion

Preferred Stock .6

Common Stock 3.0

15. Of the amount raised through sale of common stock \$390 million represented rights offerings of the chartered banks and \$472 million rights offerings of The Bell Telephone Company of Canada. Together these accounted for 28 per cent of the total net new issues of common stocks. Taken in conjunction with the taxation figures, the above show conclusively that the issuance of debt has been much greater than that of equity securities. The proportion represented by debt has fluctuated considerably from year to year, the high being 76.8 per cent in 1950 and the low 21.2 per cent in 1959 -- a year of extreme difficulty in the bond markets.



1959-1960

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Common Stock	2.0
--------------	-----

15. Of the amount raised through sale of the chartered banks and \$772 million rights offerings of The Bell Telephone Company of Canada. Together these accounted for 23 per cent of the total net new issues of common stocks. Taken in conjunction with the taxation figures, the above show conclusively that the issuance of debt has been much greater than that of equity securities. The proportion represented by debt has fluctuated considerably from year to year, the high being 76.8 per cent in 1950 and the low 21.2 per cent in 1959 -- a year of extreme difficulty in the bond markets.



1 But the average for 1949-56 was 56.3 per cent and for
2 1957-60 59.5 per cent, indicating very little change
3 from the period of sharp expansion to that of decline in
4 business capital expenditures.

5 16. Rights offerings have been a frequent
6 method of raising funds through common stock (the main
7 reason being that the preemptive rights of the share-
8 holders are protected) and these probably account for a
9 considerable proportion of the remainder of the corporate
10 stock financing. There have, however, been a number of
11 new large companies formed during the past decade, notably
12 among natural gas utilities and finance companies, which
13 have had public issues of common stock, and particularly
14 in recent years a number of smaller firms have come to
15 the market. There have also been new companies establish-
16 ed by European interests with Canadian participation
17 usually by means of participating preferred shares. On
18 the other hand, other companies have been acquired by
19 larger firms and their shares either have disappeared
20 entirely or the amount outstanding in the hands of the
21 public has been reduced substantially. One industry
22 in which this has occurred to a considerable degree is
23 pulp and paper. Thus the number of stocks listed on
24 the Toronto Stock Exchange rose only from 867 at the end
25 of 1948 to 1,117 at the end of 1961, and most of this
26 increase was in junior mining and petroleum companies.

27 UNDERWRITING

28 17. For a description of the underwriting
29 process in Canada, the following extract from "Securities
30 Regulation in Canada" by Professor J. Peter Williamson



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UNDERWRITING

17. For a description of the underwriting process in Canada, the following extract from "Securities Regulation in Canada" by Professor L. Peter Williamson



1 is essentially accurate:

2 18. "Once the underwriter is chosen, an
3 'underwriting agreement' is drawn up. Some of the
4 features of this contract are fairly standard. It will
5 usually take the form of a letter from the underwriter
6 to the issuer. The letter will describe the security
7 involved and constitute an offer to purchase the issue
8 under certain conditions. The price will probably not
9 be made definite until just before the underwriter signs
10 the letter and the issuer signs an acceptance, and this
11 will not take place until just before the offer to the
12 public. However, a price range may be tentatively
13 established at an early stage.

14 19. "The conditions set forth in the letter
15 will include some standard ones. The issuer will be
16 required to fulfill all legal requirements as to the
17 issue of the securities and as to their offer for sale
18 throughout Canada (often excepting Newfoundland and
19 Prince Edward Island). This will include compliance with
20 the applicable companies acts and the provincial
21 securities acts. The underwriter's commitment will be
22 subject to a favourable opinion of its counsel as to the
23 legality of the issue and its sale, and the issuer will
24 probably pay for this opinion.

25 20. "The accuracy of the prospectus will be
26 made the issuer's responsibility. The companies acts
27 and securities acts, where they impose liability to
28 purchasers for omissions and misstatements in a
29 prospectus, sometimes make the underwriters equally liable
30 with the issuer. Hence, the underwriting agreement will



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with the issuer. Hence, the underwriting agreement will



1 include a warranty from the issuer of the underwriter
2 that the information in the prospectus is true and that
3 the issuer consents to its use, and an indemnity to
4 protect the underwriter from the consequences of a false
5 statement, omission of a material fact, or stop order
6 issued by any securities commission.

7 21. "The issuer will be required to furnish
8 whatever financial and statistical information is
9 reasonably necessary for selling purposes, including
10 audited financial statements, if these are appropriate.

11 22. "Finally, there will be some sort of
12 escape clause, a so-called 'market out' clause. This will
13 give the underwriter an option to terminate the agreement,
14 usually up until the time the prospectus is accepted for
15 filing and a public offering may lawfully begin, in the
16 event of (to quote one such agreement) 'any catastrophe
17 of national or international effect which, in our
18 opinion (that is, the underwriter's opinion), is adverse,
19 or any action, government regulation or other occurrence
20 of any nature whatsoever which, in our opinion, seriously
21 affects or may seriously affect your business or the
22 financial markets'. It is unlikely that the clause will
23 ever be used by the underwriter. It is, after all, the
24 market rise (in a less severe form perhaps) that the
25 underwriter is being paid to take, and except in a real
26 crisis a reputable underwriter will not exercise its
27 escape rights.

28 23. It is normal practice for the issuer to
29 pay its legal expenses and for the underwriter to pay
30 its own counsel. Where one counsel acts for both, the

include a warranty from the issuer of the underwriter that the information in the prospectus is true and that the issuer consents to its use, and an indemnity to protect the underwriter from the consequences of a false statement, omission of a material fact, or stop order

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23. It is normal practice for the issuer to pay its legal expenses and for the underwriter to pay its own counsel. Where one counsel acts for both, the



1 issuer usually pays. It has been the custom for the
2 underwriter to pay for the prospectus, but the current
3 trend is towards the issuer's bearing this expense.

4 24. "Having negotiated an underwriting
5 agreement, which is as yet unsigned and lacks a final
6 price, the underwriter selects the participants for a
7 banking group. Certain underwriters may be included
8 because the issuer wants them, but the group is more
9 likely to be formed on the basis of long-standing
10 relationship with the principal underwriter. Once a
11 particular banking group has become associated in
12 financing an issuer, the members will expect to be
13 invited to participate in similar future offerings of
14 this same issuer, and the principal underwriter will
15 expect them to take up their proportionate part of
16 these new offerings.

17 25. "The principal underwriter will be a member
18 of the banking group, and its syndicate manager. The
19 name of the manager will always appear first in the list
20 of underwriters in a prospectus -- this is a mark of
21 prestige about which underwriting firms are sensitive.
22 The banking group agreement will consist of a letter from
23 the syndicate manager to each of the group members.
24 Actually 'group agreement' may be a little misleading.
25 There is no agreement among the members; each signs an
26 identical agreement (identical except for the size of the
27 participation) with the manager alone.

28 26. "The letter from the manager will give
29 a description of the securities (subject to change),
30 refer to the underwriting agreement to be signed, and

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a description of the securities (subject to change).

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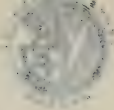


1 offer to the prospective banking group member a
2 participation of a specified amount of the issue.
3 Acceptance of the offer will constitute a purchase of
4 the participation from the manager. The banking group
5 agreement and the underwriting agreement are usually
6 signed the same day. The syndicate manager will often
7 sign the agreement with the issuer in the morning and then
8 obtain an oral acceptance by telephone from each banking
9 group member, who will mail a written acceptance the same
10 day.

11 27. "The entire letter constituting the
12 banking group agreement is pretty much standard, apart
13 from the description of the securities. The manager will
14 reserve a specified percentage of each member's
15 participation, for sales to 'exempted institutions'
16 (meaning institutional investors, such as insurance
17 companies, whom the other members agree not to solicit)
18 and to a selling group. These sales are handled
19 exclusively by the manager, selling for the accounts
20 of the banking group members. The remainder of a
21 member's participation will be sold through its own
22 facilities.

23 28. "The offering prices will be set out --
24 tentatively, until the offering day -- and depending
25 on the kind of securities offered, these may include
26 prices to the public, to exempted institutions, to various
27 dealers, and to banking group members. And the letter
28 will specify the date on which the member is required
29 to take delivery of its securities and pay for them.

30 29. "Expenses of the issue are borne by the



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29. "Expenses of the issue are borne by the



1 members in proportion to their participations, and
2 profits on sales to dealers and institutions are split
3 in the same way.

4 30. "The syndicate manager usually reserves
5 the right to 'over-allot' sales to exempted institutions
6 and to the selling group, up to 10 per cent of the total
7 offering, and to cover by purchasing on the market.
8 What this means is that the syndicate manager may
9 'stabilize' the market by allotting more than the portion
10 of the issue specifically withheld for institutions
11 and the selling group, and filling the extra orders by
12 purchasing on the market and supporting the price.
13 The other members of the selling group, of course, have
14 agreed not to solicit the exempted institutions or the
15 selling group during the period of the banking group
16 agreement. If the over-allotment results in losses,
17 the banking group shares them up to a 10 per cent over-
18 allotment.

19 31. "The next stage in the distribution is
20 the selling group. There are two ways in which the
21 syndicate manager may form a selling group. One is simply
22 to make offers to a number of dealers, which, when
23 accepted, become sales. This method may be useful
24 where the selling group is small, but the more common
25 procedure is to invite orders from selected dealers,
26 without making a commitment. The invitation is in the
27 form of a letter, called a 'selling group agreement',
28 from the manager, and is generally sent out on the day
29 registration of the securities is complete. The manager
30 opens a subscription book a day or two after the

members in proportion to their participations, and profits on sales to dealers and institutions are split in the same way.

30. "The syndicate manager usually reserves the right to 'over-allocate' sales to exempted institutions and to the selling group, up to 10 per cent of the total offering, and to cover by purchasing on the market what this means is that the syndicate manager may 'establish' the market by allocating more than the portion of the issue specifically withheld for institutions and the selling group, and filling the extra orders by purchasing on the market and supporting the price.

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invitation goes out, and accepts orders or allots proportion of orders if the demand is great.

32. "As an example, the prices on a bond purchased at 97 by the manager might be:

Retail price	\$100.00
Price to exempted institutions	100.00
Price to trust companies for resale to clients at the retail price	99.75
Price to casual dealers	99.25
Price to selling group members	98.50
Draw-down price to banking group members, and selling group members	98.50
Cost to banking group members	97.75

The difference between the \$97.75 cost to Banking Group Members and the \$98.50 draw-down price is an amount withheld by the syndicate manager to cover the expenses of the issue. Any balance of this 'holdback' not required for expenses is returned to the members. The price concession to trust companies would apply only in Quebec, where such concessions are legal.

33. "The selling group agreement, like the banking group agreement, follows a standard form. The manager signs the letter to the dealers as agent for the banking group, so that whatever contract results is between a dealer and the group. After describing the issue, the letter offers to include the addressee in a selling group, and there is a place provided for the dealer to sign in acceptance of this offer, which imposes certain obligations on him (these are discussed below). However, as to the extent of his participation,

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dealer to sign in acceptance of this offer, which

imposes certain obligations on him (these are discussed

below). However, as to the extent of his participation,



1 only an invitation is made and the banking group is
2 not bound to deliver securities until it has accepted
3 the dealer's order

4 34. "The selling group agreement repeats such
5 of the banking group agreement, including a schedule of
6 prices. The members of the selling group are required
7 to comply with securities legislation, and specifically
8 to agree not to solicit orders in the provinces where
9 the securities will not be registered or where the
10 dealer is not qualified to do business (nor to solicit
11 in the United States, unless the securities are to be
12 registered there)."

13 36. In addition to "firm commitment under-
14 writing", issues may be privately placed with one or more
15 institutions in Canada or the United States. In this
16 case the investment dealer acts simply as agent for the
17 issuer, or may do nothing more than bring two parties
18 together, using his knowledge of the investment policies
19 of various institutions. For these services the dealer
20 usually receives a moderate commission which will
21 probably range between 1/4 and 1 1/2 per cent depending
22 on how much work has been involved and the size of the
23 issue. Moreover, no registration statement is required
24 for private placements with institutions. Hence the
25 expenses of issue are lower than for a public offering.
26 On the other hand, a slightly higher yield must usually
27 be given to the lender and the covenants may be more
28 restrictive, while the company does not derive the
29 advantage of more widespread ownership (e.g. the public
30 relations aspect, and public familiarity with the

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only an invitation is made and the banking group is



1 company which may be helpful in subsequent issues of
2 securities).

3 37. Occasionally, and particularly in the case
4 of small issues, an underwriting may be on a "best
5 efforts" basis, whereby the dealer undertakes to use his
6 best efforts to sell the securities as an agent of the
7 issuer, receiving a straight commission on sales made.

8 38. A major underwriter has a twofold
9 responsibility. One is to provide sound advice to the
10 companies for which it acts as fiscal agent and underwrite
11 securities on the best terms and lowest over-all costs
12 consistent with the issuing company's financial position
13 and the condition of the securities markets. But an
14 underwriter also has an established clientele to whom
15 it sells the new issues that it underwrites or in
16 which it participates. Its reputation as an underwriter
17 is in part determined by its "placement" power. And it
18 has a responsibility to its clients to correctly
19 represent the quality of an issue and ensure that the
20 return to the investor is commensurate with the degree
21 of risk taken. As further protection to its clients and
22 to its own reputation, the underwriting house will
23 usually maintain a watching brief on the progress of a
24 company for which it acts as fiscal agent, frequently to
25 the extent of being represented on the board of
26 directors. If a company does run into difficulties the
27 underwriter often plays an active role in overcoming them,
28 occasionally placing its own resources behind the credit
29 of the company if the need arises.
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38. A major underwriter has a two-fold responsibility. One is to provide sound advice to the companies for which it acts as fiscal agent and underwriter securities on the best terms and lowest over-all costs consistent with the issuing company's financial position and the condition of the securities markets. But an underwriter also has an established clientele to whom it sells the new issues that it underwrites or in which it participates. Its reputation as an underwriter is its first asset.

has a responsibility to its clients to correctly represent the quality of an issue and ensure that the return to the investor is commensurate with the degree of risk taken. As further protection to its clients and to its own reputation, the underwriting house will usually maintain a watching brief on the progress of a company for which it acts as fiscal agent, frequently to the extent of being represented on the board of directors. If a company does run into difficulties the underwriter often plays an active role in overcoming them occasionally placing its own resources behind the credit of the company if the need arises.

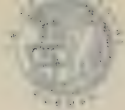
DISTRIBUTION OF BONDSTABLE III-A

Estimated distribution of holdings -
Corporate and other non-Government
Bonds

(dollar figures in thousands)

Holder	1959		1954		Change 1954/9
	Principal Amount	% of Total	Principal Amount	% of Total	
1. Bank of Canada	59	1	11		✓ 48
2. Chartered Banks	512	7	353		✓ 159
3. Provincial Governments	24	-	50		- 26
4. Municipal Governments	15	-	1		✓ 14
5. Life Insurance Companies	1924	27	1407	33	✓ 517
6. Other Insurance Companies	132	2	64		✓ 68
7. Quebec Savings Banks	21	-	16		✓ 5
8. Trust & Mortgage Loan Co.	160	2	81		✓ 79
9. Pension Plans	473	7)	742		✓ 1062
10. All other Residents	1331	19)			
11. Total Residents	4651	65	2725	65	✓ 1926
12. Non Resident	2479	35	1498	35	✓ 981
	7130	100	4223	100	✓ 2907

Source: Bank of Canada Statistical Summary Supplement
1960.



DISTRIBUTION OF BONDS

TABLE 21-1

Estimated distribution of holdings -
Corporate and other non-government

(dollar figures in thousands)

1954	Principal & of	Principal & of	Principal & of
1954	1954	1954	1954
1. Bank of Canada	50	1	
2. Provincial Governments	25	353	4 159
3. Provincial Governments	24	50	- 26
4. Provincial Governments	15	1	4 14
5. Provincial Governments	100	1407	33 4 517
6. Provincial Governments	135	64	4 68
7. Provincial Governments	21	16	4 51
8. Trust & Mortgage Loan Co.	160	81	4 79
9. Pension Plans	473		
10. All other Residents	1331		
11. Total Residents	457	275	65 4 1026
12. Non Resident	2479	1450	35 4 981
	7130	4223	100 4 2007



38A. From the foregoing it can be observed that (1) domestic institutions and pension funds comprise the largest market for corporate bonds, accounting in 1959 for some \$3,320 millions principal amount equivalent to roughly 46.5 per cent of outstanding corporate debt obligations, (2) the life insurance industry is the largest single market for corporate bonds, and (3) non-residents have acquired roughly 35 per cent of Canadian corporate and other bonds. The (life) insurance industry in 1959 owned \$2,056 millions principal amount of corporate bonds, equivalent to approximately 29 per cent of the total outstanding principal amount of Canadian corporate and other bonds. In 1954 however, this industry owned \$1,471 millions principal amount of corporate bonds, equivalent at that time to roughly 35 per cent of the total outstanding principal amount of Canadian corporate and other non-government bonds.

38B. This trend is significant for the investment dealer as it points out that problems in the distribution of corporate bonds are becoming more complex; for though there are several large buyers, in itself a factor tending to somewhat simplify the distribution process, the reduction in the leading role of the insurance industry requires the investment dealer to turn to several other sources.

38C. In passing it is worth noting that the insurance industry in the United States of America is a much more dominant factor in the acquisition of corporate bonds than the life insurance industry is in Canada. To this extent therefore the Canadian investment dealer has

the largest market for corporate bonds, accounting in 1959 for some \$3,350 million principal amount equivalent to roughly 46.5 per cent of outstanding corporate debt obligations. (2) the life insurance industry is the largest single market for corporate bonds, and (3) non-residents have acquired roughly 35 per cent of Canadian corporate and other bonds. The (1959) insurance industry in 1959 owned \$2,056 million principal amount of corporate bonds, equivalent to approximately 29 per cent of the total outstanding principal amount of Canadian corporate and other bonds. In 1954 however, this industry owned \$1,471 million principal amount of corporate bonds, equivalent at that time to roughly 35 per cent of the total outstanding principal amount of Canadian corporate and other non-government bonds.

384. This trend is significant for the investment dealer as it points out that problems in the distribution of corporate bonds are becoming more complex for though there are several large buyers, in itself a factor tending to somewhat simplify the distribution process, the reduction in the leading role of the insurance industry requires the investment dealer to turn to several other sources.

385. In passing it is worth noting that the insurance industry in the United States of America is a much more dominant factor in the acquisition of corporate bonds than the life insurance industry is in Canada. To this extent therefore the Canadian investment dealer has



1 a more complex distribution problem than his U.S.
2 competitor.

3 38D. Table III-A, pointing out that 35 per
4 cent of Canadian corporate and other bonds are in the
5 hands of non-residents, indicates the desirability of
6 access to foreign capital markets if the investment
7 dealer is to continue to fulfill his functions of raising
8 capital funds for business enterprise.

9 UNDERWRITING COSTS

10 39. The cost of issuing securities varies
11 according to two main factors -- size and degree of risk.
12 With regard to size there are certain expenses involved
13 such as legal fees, preparation of prospectus, research
14 and sales expenses which are more or less fixed
15 regardless of the size of an issue. Thus the smaller
16 the issue, the larger is the relative burden of these
17 charges. In the matter of risk, the underwriter assumes
18 a greater chance of loss on securities of small or new
19 companies, or those with unstable earnings records,
20 than with, for example, a well established utility; the
21 chance of loss is also greater in the underwriting of
22 junior securities, particularly common stocks, than in
23 the case of first mortgage bonds. These factors account
24 in large measure for the differences in costs shown in
25 the following table, derived from reports submitted by
26 members of the Investment Dealers' Association.



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III. COST OF ISSUING SECURITIES

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a greater chance of loss on securities of small or new

companies, or those with unstable earnings records,

than with, for example, a well established utility; the

chance of loss is also greater in the underwriting of

junior securities, particularly common stocks, than in

the case of first mortgage bonds. These factors account

in large measure for the differences in costs shown in

the following table, derived from reports submitted by

members of the Investment Dealers' Association.

TABLE IV

Number of Members Reporting	Percentage		
	Arith- metic Average	Median	Range
Average gross mark up (as a per cent of cost) on -			
Common stock issues -			
(a) under \$3 million	24	8.43	9.09 2.00 - 14.00
(b) over \$3 million	7	6.98	6.38 5.00 - 10.00
Preferred stock -			
(a) under \$3 million	14	6.05	4.77 3.50 - 11.11
(b) over \$3 million	6	4.75	4.00 3.50 - 6.50
Bonds and Debentures			
(a) under \$3 million	33	4.62	3.90 1.00 - 10.00
(b) over \$3 million	20	2.82	2.85 .50 - 5.00

COMPARISON WITH THE UNITED STATES

40. In general, and this belief arises in good part from our experience in joint underwritings with U.S. firms on Canadian issues, we would say that costs are very similar in the two countries, but generally somewhat higher in Canada for large issues and somewhat lower for small issues. A study by the Securities and Exchange Commission in 1957 produced the following data:



TABLE 1

Number of firms

in each

category

of firms

in each

category

of firms

in each

category

of firms

in each

category

of firms

in each

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of firms

in each

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similar in the two countries, but generally somewhat
higher in Canada for large issues and somewhat lower for
small issues. A study by the Securities and Exchange
Commission in 1957 produced the following data:



TABLE V

United States Underwriter's Compensation %
of Gross Proceeds of New Issue (1951, 1953
and 1955).

<u>\$ millions)</u> <u>Size of Issue</u>		<u>Common</u> <u>Stock</u>	<u>Preferred</u> <u>Stock</u>	<u>Bonds, Notes,</u> <u>Debentures</u>
under	.5	27.15%	-	-
.5	.9	21.76	12.63	11.49
1	- 1.9	13.58	8.07	8.17
2	- 4.9	9.97	4.88	3.78
5	- 9.9	6.17	3.72	1.83
10	- 19.9	4.66	2.92	1.52
20	- 49.9	5.37	3.20	1.33
50 and over		-	2.51	1.19

N.B. The percentages given above are the arithmetic
averages in each classification.

41. The data in Table V are subdivided into
more classes than the information requested from members
of the I.D.A. and show clearly the tendency for under-
writing costs to decline with the size of the issue and
the type of security issued. Other data in the S.E.C.
study also show a correlation between the size of the
issuing company and the underwriting costs.

42. In comparing Table IV with Table V, it
must be noted that the former is the gross mark up as
a percentage of cost, whereas the latter is expressed as
a percentage of the issuing price. If the Canadian
data were on a comparable basis with the U.S., the
percentage would therefore be somewhat lower. Even
so, it is apparent that in issues of under \$3 millions
underwriting costs are lower in Canada than in the U.S.,
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1 significantly lower), while for larger issues they are
2 a point or so higher.

3 43. Further support for this conclusion can
4 be found in a comparison of the spread between yield to
5 buyer and yield cost to company of utility issues rated
6 by Moody's. In 1959 and 1960 such spreads on issues
7 by U.S. utilities rated by Moody's as BA or BAA ranged
8 from .0 per cent to .17 per cent; issues of Canadian
9 utilities with similar ratings in recent years have had
10 spreads ranging from .11 per cent to .17 per cent (in
11 both cases the issues surveyed were in excess of \$15
12 million). A further sample of large issues of well
13 regarded Canadian companies, but not rated by Moody's,
14 showed spreads from .16 per cent to .18 per cent. In
15 this comparison we have used "yield spread" as this was
16 the information supplied in Moody's Public Utilities
17 Manual.

18 44. There are, of course, fundamental
19 differences in the nature of the markets in the two
20 countries. The very size of the major financial
21 institutions in the United States makes it possible for
22 issues even as large as \$50 million to be placed with
23 only a handful of buyers and retail distribution of
24 bonds to individuals is the exception rather than the
25 rule. In Canada, by contrast, most issues are sold to
26 a large number of institutions and individuals. The
27 costs of distribution are therefore considerably higher
28 in this country, and do not fall as rapidly with size
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1 COMPETITIVE BIDDING versus NEGOTIATED SALES

2 45. The comparison between comparable U.S. and
3 Canadian utilities in Paragraph 43 is interesting for in
4 many cases U.S. utilities are compelled by the regulatory
5 authorities to call for competitive bids on new debt
6 security issues, whereas in Canada the practice amongst
7 non-Government companies is to have negotiated issues
8 with fiscal agents.

9 46. The theory behind competitive bidding in
10 new issues, as with other types of contract, is that
11 competition is likely to result in the most favourable
12 price to the seller. In some instances this probably
13 holds true. There is reason to believe, however, that
14 this may not be so in the case of security issues,
15 judging by the experience in the United States.

16 47. From the data supplied in Moody's Public
17 Utility Manual, a comparison was made of negotiated sales
18 and competitive tenders, taking issues with the same
19 rating, issued at roughly the same time of year (i.e.
20 within the same month) and of approximately the same
21 size. In total, 16 comparable pairs of issues that
22 fitted these requirements during 1959 and 1960 were
23 found. In 11 of these comparisons both the yield to
24 the public and the yield cost to the borrowing company
25 were lower in the case of negotiated sales than in
26 competitive bidding, while in 5 they were higher. The
27 spread between yield to buyer and yield cost to borrower,
28 representing the underwriting spread, was lower for
29 negotiated sales in six comparisons, the same in 3 and
30 higher in 7. With regard to the degree of difference,



COMPETITIVE BIDDING WITH NEGOTIATED SALES

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46. The theory behind competitive bidding in new issues, as with other types of contracts, is that competition is likely to result in the most favourable terms to the issuer. There is reason to believe, however, that this may not be so in the case of security issues. Judging by the experience in the United States,

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1 in the 11 cases where the yield cost to the borrowing
2 company was lower for negotiated sales, the average
3 difference from competitive bids was .29 basis points;
4 in the five cases where competitive bids showed a lower
5 yield cost, the difference averaged .11 basis points.

6 48. It would perhaps be unwise to draw strong
7 conclusions from this limited survey, but there are good
8 reasons why negotiated sales should in fact be cheaper
9 for the issuing company than competitive bids. For
10 a fiscal agent maintains a continuous relationship with
11 a company. It is in a position to advise on the nature
12 and timing of new issues, can assist in the preparation
13 of the prospectus and can test the market ahead of time
14 in order to ensure that the terms of the issue will be
15 attractive to potential buyers, but not so attractive as
16 to add unnecessarily to the borrower's cost. The fiscal
17 agent tends to serve as an adviser in other matters
18 relating to corporation finance, such as the temporary
19 investment of funds and purchase of bonds for sinking
20 funds, and also maintains markets for securities between
21 issues. Where competitive bidding is followed, on the
22 other hand, the terms of an issue are drawn up by the
23 company, although sometimes a consultant is hired to
24 advise on the issue and prepare supporting data, and
25 dealers are required to bid on short notice without
26 benefit of advance preparation and without a full and
27 detailed knowledge of the company's position.
28 Particularly when interest rates are on a rising trend,
29 dealers therefore tend to allow fully for unforeseen
30 problems when submitting bids.



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1 48A. The considered opinion of Judge Medina
2 on this effect of competitive bidding was that:

3 "Fundamentally, the contentions of
4 government counsel on this and other
5 phases of the case stem from a mis-
6 conception of the investment banking
7 business. And yet the advantages to
8 an issuer, which are incidents of a
9 continuing relationship with a good
10 investment banker, seem too obvious for
11 comment. In every business the
12 customer feels that there are cogent
13 reasons why he should continue with
14 the firm which has rendered good service
15 in the past. But with a series of
16 security issues, the saving in the time
17 and labour of the officers and employees
18 of an issuer, which would have to be
19 spent in teaching a new investment
20 banker the intricacies of the business,
21 and the financial set up of the company,
22 are a matter of real consequence; and
23 it must not be forgotten that many of
24 the matters to be discussed are of such
25 a character that company officials desire
26 to have such conversations only with
27 those whom they trust, and in whose
28 integrity and competence they have
29 complete confidence."

30 49. As mentioned previously, it is the practice



48A. The considered opinion of Judge Madson

on this effect of competitive bidding was that:

"Fundamentally, the contents of government counsel on this and other phases of the case stem from a misconception of the investment banking business. And yet the advantages to an issuer, which are incidents of a continuing relationship with a good investment banker, seem too obvious for comment. In every business the customer feels that there are cogent reasons why he should continue with the firm which has rendered good service in the past. But with a series of security issues, the saving in the time and labour of the officers and employees of an issuer, which would have to be spent in teaching a new investment banker the intricacies of the business, and the financial set up of the company, are a matter of real consequence; and it must not be forgotten that many of the matters to be discussed are of such a character that company officials desire to have such conversations only with those whom they trust, and in whose integrity and competence they have complete confidence."

49. As mentioned previously, it is the practice



1 in Canada for most companies to have fiscal agents. There
2 is nothing to prevent a company from calling for bids
3 on its issues should it so desire, but it is generally
4 recognized that any advantages of this are outweighed
5 by the disadvantages.

6 AMORTIZATION OF UNDERWRITING EXPENSES

7 50. When a company issues debt securities, the
8 usual practice is to capitalize the difference between
9 the par value of the debt issued and the net amount
10 received from the underwriters, and gradually write off
11 the bond discount and expenses so created by appropriate
12 charges to earnings over the life of the security or at
13 once to earned surplus. Such charges, however, are not
14 deductible from income for tax purposes. To the extent
15 that the difference between par value and net receipts
16 of funds represents the sale of bonds to the public at
17 less than par value, it is reasonable that the
18 amortization charges should not be tax deductible. But
19 to the extent that it represents the underwriters'
20 commission, we feel very strongly that it is fair and
21 reasonable that the charges should be allowed as a
22 deductible item, for the cost of raising funds is just
23 as much a cost of doing business as, for example, the
24 fee paid to an engineering consultant. We therefore
25 suggest that the income tax legislation be amended so as
26 to permit companies to deduct underwriting costs in
27 arriving at taxable income.

28 SECURITIES LEGISLATION

29 51. Securities regulation in Canada involves
30 ten provincial Securities Acts, various provincial



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1 Companies Act, the Dominion Companies Act, the Ontario
2 Corporation Information Act and the Quebec Companies
3 Information Act. The movement towards bringing some
4 uniformity and order to this mass of legislation is
5 proceeding slowly but progress has been noted. For
6 example, the provinces are currently studying a uniform
7 Companies Act; four provinces now have identical, or
8 nearly identical, Securities Acts, and it is understood
9 that two other provinces are in the process of adopting
10 very similar Securities Acts.

11 52. The Association has for some years been
12 suggesting to provincial officials the advisability and
13 the advantages to the provinces and the investing public
14 of enacting uniform securities legislation and of
15 administering such legislation in a uniform manner and
16 observes that definite progress has been achieved in
17 this regard. The Association recommends that steps
18 should be taken whereby all provinces will expedite
19 registration of new issues of investment securities on a
20 uniform basis.

21 53. The Association has noted with interest
22 a proposal that a Federal Securities Act and a Federal
23 Securities Commission be established. The United
24 States has two Federal Acts: The Securities Act of
25 1933, which is a full disclosure statute permitting the
26 sale of a security provided specified information is
27 given to the purchaser, and The Securities Exchange Act
28 of 1934, which is primarily concerned with trading in
29 securities after the primary offering. The 1934 Act
30 regulates stock exchanges, the registration of brokers



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1 and dealers and imposes reporting, proxy and trading
2 conditions relating to securities listed on stock
3 exchanges. It should be observed that, in addition to
4 these two Federal Statutes, 48 states also have
5 securities legislation.

6 54. It would appear to the Association that
7 if a Federal Securities Act and Commission were ever
8 to come into being in Canada they would be superimposed
9 on but would not replace the existing provincial
10 securities legislation and commissions. The Association
11 recommends that S.E.C. - type legislation not be
12 established in Canada and that the Royal Commission take
13 note of the progress which has already been achieved
14 towards uniform securities legislation uniformly
15 administered as well as the work in this connection
16 which is presently in progress.

17 55. However, as the acts now stand, it is
18 necessary that a complete prospectus be in the hands of
19 a prospective buyer before an issue can be sold to him.
20 Exceptions to this rule are the chartered banks, life
21 insurance companies and trust companies. It would be
22 helpful if the practice in the United States of using
23 a "red herring" could be followed here. This is
24 essentially a preliminary prospectus, with all the
25 details except price and yield, which is distributed
26 pending approval of the regulatory authorities. The
27 institutions and other prospective buyers can study this
28 at their leisure and indicate, subject to approval of
29 the prospectus by the authorities and to the terms of
30 the issue being satisfactory, how much they would be

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1 prepared to purchase. This makes for more orderly
2 marketing of the issue, as it gives the syndicate manager
3 an indication of the requirements of major buyers and
4 participating dealers, and at the same time gives the
5 buyer more time in which to appraise the issue, without
6 in any way negating the purpose of the present require-
7 ment that a buyer see a final prospectus before he buys.
8 We would recommend that the various acts be amended to
9 permit this practice in Canada.

10 56. It would also be helpful if all
11 regulations affecting the underwriting and sale of
12 securities were promulgated to the Investment Dealers'
13 Association, who would then inform all its members. At
14 the present time, regulations are frequently not
15 publicized and they are not discovered, or their import
16 not fully appreciated, until the regulatory authorities
17 bring them to the attention of an underwriter in a
18 particular case. This, too, can result in delay in
19 the scheduling of a new issue.

20 57. The expropriation of electric utilities
21 by provinces have in the past and can in the future
22 provide a heavy blow to the very foundation of Canadian
23 justice. In the case of the B.C. Electric Company, the
24 IDAC strongly asserted that in the interests of justice
25 provisions should be made for arbitration and independent
26 appraisal of expropriated assets. It would seem
27 desirable that insofar as is possible the justification
28 for expropriating utilities should be removed. It thus
29 seems essential that the Commission should give careful
30 consideration to this question with a view to making a



prepared to purchase. This makes for more orderly marketing of the issue, as it gives the syndicate manager an indication of the requirements of major buyers and participating dealers, and at the same time gives the buyer more time in which to appraise the issue, without in any way negating the purpose of the present requirement that a buyer see a final prospectus before he buys. We would recommend that the various acts be amended to permit this practice in Canada.

56. It would also be helpful if all regulations affecting the underwriting and sale of securities were promulgated to the Investment Dealers' Association, who would then inform all its members. At the present time, regulations are frequently not publicized and they are not discovered, or their import not fully appreciated, until the regulatory authorities bring them to the attention of an underwriter in a particular case. This, too, can result in delay in the scheduling of a new issue.

57. The expropriation of electric utilities by provinces have in the past and can in the future provide a heavy blow to the very foundation of Canadian justice. In the case of the B.C. Electric Company, the IDAC strongly asserted that in the interests of justice provisions should be made for arbitration and independent appraisal of expropriated assets. It would seem desirable that insofar as is possible the justification for expropriating utilities should be removed. It thus seems essential that the Commission should give careful consideration to this question with a view to making a



1 recommendation that the Federal Government do all that
2 is in its power to devise means of removing the
3 temptations to expropriate which arise out of the Federal
4 Tax treatment of the provinces. Any such action would
5 contribute to the restoration of the shaken confidence
6 of Canadian and foreign investors in investing in
7 electric utilities in particular and private industry
8 in general.

9 58. In the matter of mergers and amalgamations
10 there appears to be an absence of adequate safeguards
11 to provide proper protection for what should be the
12 rights of shareholders. Under conditions in which Canada
13 is struggling to compete in world markets mergers may
14 be desirable. As many Canadian businesses are small in
15 comparison to their foreign competitors, certain mergers
16 may well enable Canadian business to compete more
17 efficiently and effectively and foster progress for this
18 country. However, while recognizing the values of
19 mergers or similar amalgamations when soundly conceived
20 and properly organized, the IDAC deplors the so-called
21 "take-over" technique when: (a) the identity of the
22 buying principal is not disclosed; (b) the offer, if
23 for less than 100 per cent of the voting stock, is not
24 made proportionately to all shareholders; (c) the term
25 of the offer is not sufficiently long to give all
26 shareholders reasonable time to consider it.

27 59. Speaking generally, a company incorporated
28 under the Companies Act of Canada is the natural vehicle
29 to carry on a corporate enterprise in several provinces
30 and is more attractive to foreign investors than a

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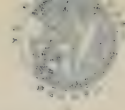


provincially incorporated company. However, the Act contains certain anomalies which tend to deter the incorporation of companies under its provisions and create unnecessary delays, expense and inconvenience in connection with the securities of companies which are incorporated under it. It is submitted that the Act should be reviewed with a view to elimination of these anomalies. In particular, it is recommended that private companies be permitted to offer their bonds and debentures to institutional investors, that the redemption and purchase for cancellation of preferred shares be simplified, that, in proper cases, companies incorporated under the Act be exempt from issuing and filing a prospectus in connection with the sale of their securities, that section 128, relating to the compulsory sale of shares, be repealed and that the Act be amended to permit amalgamation of Dominion companies either with other Dominion companies or with companies incorporated under the laws of any one of the provinces.

CORPORATION FINANCE

CONCLUSIONS AND RECOMMENDATIONS FOR THE I.D.A. BRIEF

<u>References</u>	
	Reflecting the importance of internally
Para. 4,7,	generated funds, which appear to have
8-11	financed approximately 60 per cent of the
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CONCLUSIONS AND RECOMMENDATIONS FOR THE I.D.A.

Reflecting the importance of internally generated funds, which appear to have financed approximately 60 per cent of the total applications of funds of Canadian business during the period 1949-59, there has been very little weakening in the financial structure of business. Nevertheless, the trend towards a higher proportion

References
Para. 4.7.
8-11



1 of debt in the structure of capitalization
2 is apparent. Among the factors influencing
3 this is the high rate of corporate income
4 tax, which provides an incentive for
5 unsound financing.

6 Para.
40-44

Underwriting costs appear to be lower in
7 Canada than in the United States for small
8 issues and somewhat higher for large
9 issues. Because of the different nature of
10 the markets in the two countries, distrib-
11 ution costs do not fall as rapidly with size
12 in Canada as in the United States.

13 Para 50.

It is recommended that income tax legislation
14 be amended so as to permit companies to
15 deduct underwriting costs in arriving at
16 taxable income.

17 Para.54

It is recommended that S.E.C.-type
18 legislation be not established in Canada and
19 that the Commission take note of the progress
20 already achieved towards uniform securities
21 legislation uniformly administered and the
22 work presently in progress to achieve this
23 objective.

24 Para. 55

It is recommended that the various
25 securities acts be amended so as to permit
26 the distribution of preliminary prospectuses
27 in order that prospective buyers of a new
28 issue can study it at length and indicate,
29 subject to approval of the prospectus by
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Para. 49

Para 50

Para. 54

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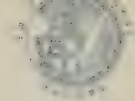
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15 ing that the Federal Government devise means
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APPENDIX FSECONDARY BOND MARKETI N D E X

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10-11	II.	Origin of Secondary Markets in Canada	A.386
12-29	III.	The Secondary Bond Market today.	A.387
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18-21		(b) Regulation of Secondary Markets	A.393
22		(c) Capital and Margin Requirements	A.395
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52-53	VI.	Market Data, Availability and Adequacy.	A.413
54-59	VII.	Consideration of a Bond Exchange	A.414
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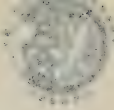
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BRIEF OF THE TRADING FUNCTIONS COMMITTEE

For the purpose of this brief the following definitions will apply:

Broker	Member of a recognized stock exchange
Dealer	Member of the Investment Dealers Association of Canada or others such as Chartered Banks who participate in the secondary bond market.
Agent	Dealer who acts as a intermediary between buyer and seller at an established price and receives a commission for his services.
Principal	A dealer who accepts liability for his own account through either the purchase or sale of securities. It should be noted that dealers customarily act both as agent and principal but not in the same transaction and any purchase or sale must be designated as one or the other.
Money Market Dealer	One of 14 member dealers of the Investment Dealers Association to have been extended lines of credit by the Bank of Canada to facilitate their functions in the handling of Government of Canada Treasury Bills, and Government of Canada and Guaranteed Bonds with a maturity of less than 3 years.
Depth	The secondary market has depth when there are actual or easily accessible orders both above and below the current level of prices. A market lacking depth would be shallow.
Breadth	The secondary market has breadth when orders are in volume and from widely divergent groups of investors. A market lacking breadth would be narrow.
Resilience	The secondary market has resilience when new orders come into the market in volume in response to perceptible changes in yield. A synonym would be elastic and a market lacking resilience would be inelastic.
Thin	Describes a market which lacks depth, breadth and resilience.
Position	The liability which a firm has incurred in any security. The total of all



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	The liquidity which a firm has borrowed in any security. The total of all



positions of a firm would make up that firm's inventory. A long position is one in which the firm has purchased securities for future sale. A short position is one in which the firm has sold securities which it does not currently own but which are to be purchased at a later date.

---O---

I. THE NEED FOR A SECONDARY MARKET

1. It is inherent in the nature of a highly-developed capitalist society that there must be a mechanism by which capital may change hands. The process of transferring new capital from a saver to a user takes place in what is known as a primary market; while the transfer of outstanding (previously issued) securities from one investor to another takes place in the secondary market. In this brief we are concerned with the secondary bond market and will mention primary markets only where they impinge on the main subject.

2. The importance of the secondary market to the continuing development of the economy cannot be over-emphasized, for this market is a vital factor in regulating the smooth and efficient flow of funds from savers to users. There is no doubt that lack of secondary markets would increase the cost of capital and, by inhibiting the mobility of funds, reduce the ability of the country to finance its development from domestic sources.

3. Secondary markets provide two basic functions -- value perspective and liquidity -- on which the system depends for the orderly use of capital.



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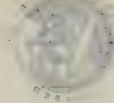
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1 Through the secondary market, a level of prices is
2 established which gives borrowers a reliable indication
3 of the cost of capital and lenders an estimate of the
4 rate of return they might expect from the type and terms
5 of security being offered. This method provides the
6 logical means of arriving at fair value for both parties.
7 By establishing relative values at any point in time,
8 secondary markets assist in establishing the order of
9 preference in which prospective issuers will be allotted
10 funds. The market is, therefore, an important factor
11 in regulating the flow of capital throughout the
12 economy.

13 4. The degree of liquidity which any new
14 issue of bonds is likely to enjoy is second only to fair
15 pricing in the minds of most investors. The secondary
16 market provides the yardstick by which liquidity may be
17 gauged from the behaviour of comparable outstanding
18 issues. Investors having mandatory requirement for the
19 return of cash at specific dates, purchase securities
20 tailored to their needs. Others, who are unaware at
21 time of purchase of future requirements for the return
22 of cash, may purchase bonds having an intermediate or
23 long term maturity in order to obtain the greater yield
24 usually available. Conditions may arise whereby these
25 investors desire to sell their holdings and the
26 secondary market provides the means of so doing.
27 Without liquidity, investors would be more reluctant to
28 advance funds, borrowing costs would be substantially
29 higher, and users would pay an unduly high price for
30 capital. Markets also afford users the opportunity to



Through the secondary market, a level of prices is established which gives borrowers a reliable indication of the cost of capital and lenders an estimate of the rate of return they might expect from the type and terms of security being offered. This method provides the desired amount of information to both sides of the market. The market is, therefore, an important factor in regulating the flow of capital throughout the economy.

4. The degree of liquidity which any new issue of bonds is likely to enjoy is a good guide to pricing in the minds of most investors. The secondary market provides the yardstick by which liquidity may be gauged from the behavior of comparable outstanding issues. Investors having mandatory requirements for the return of cash at specific dates, purchase securities tailored to their needs. Others, who are uncommitted to the purchase of future requirements for the return of cash, may purchase bonds having an intermediate or long term maturity in order to obtain the greater yield usually available. Conditions may arise whereby these investors desire to sell their holdings and the secondary market provides the means for so doing. Without liquidity, investors would be more reluctant to advance funds, borrowing costs would be substantially higher, and there would be no opportunity to



1 carry out Sinking Fund and Purchase Fund operations at
2 fair prices.

3 5. The importance of liquidity in reducing
4 the costs of borrowing is made evident by comparison
5 with mortgage rates in Canada. In the majority of
6 cases, the cost of raising capital through a conventional
7 mortgage is higher than that which would apply to an
8 issue of bonds or debentures by the same issuer. Although
9 other additional service charges must be considered, it
10 is generally conceded that the higher interest cost of
11 mortgages is largely due to the lack of an effective
12 secondary market in which the investor may regain his
13 funds for other purposes.

14 6. Open market purchases or sales by Bank of
15 Canada in accordance with its interpretation of
16 requirements for the conduct of monetary policy and
17 other necessary movements of securities are greatly
18 facilitated by the secondary market. Chartered Banks,
19 Trust Companies, Corporations and individuals also rely
20 on the market for portfolio adjustment.

21 7. The figures shown below compare total new
22 bond issues in Canada during 1961 with the additional
23 volume of secondary market sales made by members of
24 the I.D.A.C. during their fiscal year. Not included
25 are sales made by Bank of Canada, Chartered Banks or
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27
28
29
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are sales made by Bank of Canada, Chartered Banks or

other participants in the secondary market.



TABLE I

Primary Market Sales vs. Secondary Market
Sales, 1961 000's of Dollars

	Primary Market (1) Sales	Secondary Market (1) Sales
Treasury Bills	6,240,000	6,142,159 (4)
Canadas and Guarantees:		
under 3 years	1,325,000(3)	4,618,820
over 3 years	875,000(3)	1,961,748
Provincials and Guarantees:		
public sale	9,000	
parity & Savings bonds	204,645	
Municipals	462,180/	368,087
Corporate, public sale	418,460	1,400,230
private sale	248,050	
	10,520,386	15,780,048
Less	1,015,000(3)	
	<u>9,505,386</u>	

(1) Source: Financial Post Record of Financing in 1961.
(January and February, 1962).

(2) Source: I.D.A.C.

(3) Of the Primary Market Sales, the following gross amounts were taken by Bank of Canada and paid for by surrender of other maturing debt. Substantial amounts were later distributed to the public through the secondary market.

Canadas, under 3 years	\$ 440,000,000
Canadas, over 3 years	\$ <u>575,000,000</u>
	<u>\$1,015,000,000</u>

(4) Bills purchased by dealers at Thursday auctions are included. Purchase and re-sale agreements are not shown.

8. Although the secondary market sales of I.D.A.C. members only are shown, the total volume represents 166 per cent of primary market sales.



TABLE I

Primary Market Sales of Government Securities
Sales, 1961 000's of Dollars

Secondary Sales	Primary Sales	
6,240,000	6,240,000	Treasury Bills
1,325,000(3)	1,325,000(3)	over 3 years
4,618,820	4,618,820	under 3 years
875,000(3)	875,000(3)	over 3 years
204,645	204,645	Provincials and Guarantees:
9,000	9,000	public sale
195,645	195,645	private & savings bonds
358,087	358,1804	Municipals
1,400,220	1,418,460	Corporate, public sale
	248,050	private sale
12,780,048	10,220,386	
	1,015,000(3)	Less
	9,205,386	

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8. Although the secondary market sales of I.D.A.C. members only are shown, the total volume represents 100 per cent of primary market sales.



1 Excluding Treasury Bills the figure would be 295 per
2 cent.

3 9. It is of interest that approximately 95
4 per cent of the total recorded volume was handled by 33
5 dealers who carried inventories of over \$1 million. If
6 sales of Treasury Bills were excluded the proportion
7 would be about 92 per cent. (Reference Table 3).

8 II. ORIGIN OF SECONDARY MARKETS IN CANADA

9 10. At the turn of the century there was to
10 all intents and purposes no broad securities market
11 in Canada and, in fact, as far as debt securities were
12 concerned this condition existed up to the advent of
13 the First World War. Prior to 1914 almost all Canadian
14 capital requirements were met by imports from the United
15 Kingdom and, after 1914, by imports from the United
16 States. It was not until the U.S. market was restricted
17 by the entry of the Americans into the war in 1917
18 that Canadians were faced with financing the major share
19 of their own capital requirements. During the period
20 prior to 1917 there were markets being made in
21 Canadian debt securities in London and New York but lack
22 of an efficient market system in Canada, coupled with
23 poor communications, did not provide the domestic
24 investor with a satisfactory means of buying or selling
25 bonds. The Victory loans, first offered to the public
26 in 1917, brought about the necessity for the establish-
27 ment of a secondary market as a substantial volume of
28 bonds had been placed domestically.

29 11. As early as 1914, the Bond Dealers
30 Section of the Toronto Board of Trade had been formed and

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II. ORIGIN OF SECONDARY MARKETS IN CANADA

10. At the turn of the century there was to all intents and purposes no broad securities market in Canada and, in fact, as far as debt securities were concerned this condition existed up to the advent of the First World War. Prior to 1914 almost all Canadian capital requirements were met by imports from the United Kingdom and, after 1914, by imports from the United States. It was not until the U.S. market was restricted by the entry of the Americans into the war in 1917 that Canadians were faced with financing the major share of their own capital requirements. During the period prior to 1917 there were markets being made in Canadian debt securities in London and New York but lack of an efficient market system in Canada, coupled with poor communications, did not provide the domestic investor with a satisfactory means of buying or selling bonds. The Victory loans, first offered to the public in 1917, brought about the necessity for the establishment of a secondary market as a substantial volume of bonds had been placed domestically.

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1 in 1916 dealers in Montreal became interested in an
2 association which resulted in the amalgamation of the two
3 into the Bond Dealers Association of Canada. This group,
4 the predecessor of the present I.D.A.C., originally
5 consisted of 32 dealers from Montreal and Toronto. By
6 1919 the Association had grown to 72 members, including
7 some from Western Canada and the Maritimes, and an
8 active secondary market had begun to develop. This
9 market developed actively during the 1920's and 1930's
10 but was relatively stagnant during World War II.
11 However, with the enormous expansion of the economy in
12 the post-war period, the demand for capital grew very
13 quickly, resulting in a highly-developed, vigorous
14 secondary bond market.

15 III. THE SECONDARY BOND MARKET TODAY

16 (A) How Markets are Made

17 12. Those who normally participate in the
18 secondary bond market as it is presently constituted are
19 members of the I.D.A.C.; Trading Departments of the
20 Chartered Banks and the Securities Department of Bank of
21 Canada. In addition, members of the various Stock
22 Exchanges in Canada and a number of other brokers and/or
23 dealers licensed to deal in securities with the public
24 by Provincial Securities Commissions may participate
25 but experience has shown limited activity by these
26 groups. The number in each category:



in 1916 dealers in Montreal became interested in an association which resulted in the amalgamation of the two into the Bond Dealers Association of Canada. This group the predecessor of the present I.D.A.C., originally consisted of 32 dealers from Montreal and Toronto. By 1919 the Association had grown to 72 members, including some from Western Canada and the Maritimes, and an active secondary market had begun to develop. This market developed actively during the 1920's and 1930's. However, with the enormous expansion of the economy in the post-war period, the demand for capital grew very quickly, resulting in a highly-developed, vigorous

III. THE SECONDARY BOND MARKET TODAY

(A) How Markets are Made

12. Those who normally participate in the secondary bond market as it is presently constituted are members of the I.D.A.C.; Trading Departments of the Chartered Banks and the Securities Department of Bank of Canada. In addition, members of the various Stock Exchanges in Canada and a number of other brokers and/or dealers licensed to deal in securities with the public by Provincial Securities Commissions may participate but experience has shown limited activity by these groups. The number in each category:



TABLE 2

Members of the I.D.A.C.	185
Chartered Banks	8
Bank of Canada	<u>1</u>
Total	<u>194</u>
Members of Toronto, Montreal and Canadian Stock Exchanges (non I.D.A.C.)	45
Other licensed brokers and/or dealers, not included above (1)	200-250

(1) Source: I.D.A.C.

13. These dealers participate to a widely varying degree. The large majority makes use of the market only to execute orders obtained from clients and in most cases should therefore be described as agents. Others, while acting as agent in certain transactions, normally act as principals, buying and selling for their own account. From the results of a survey based on figures for 1961, presented in Table 3, there are 16 dealers who customarily maintained total positions in excess of \$5,000,000 and 17 dealers whose positions were between \$1,000,000 and \$5,000,000. These dealers are, generally speaking, responsible for the origination and maintenance of secondary market levels. It is only through the willingness of such dealers to assume liabilities for their own risk that a continuing market without unduly sharp fluctuations can be achieved.

14. Table 4 summarizes inventory positions of members on a quarterly basis during 1961 by class of securities. Both long and short positions are shown and it is of interest to note the frequency with which short

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dealers who customarily maintained total positions in figures for 1961, presented in Table 3, there are 16 own account. From the results of a survey based on normally act as principals, buying and selling for their Others, while acting as agent in certain transactions, in most cases should therefore be described as agents, market only to execute orders obtained from clients and varying degree. The large majority makes use of the

13. These dealers participate to a widely (1) Source: I.D.A.C.

dealers, not included above (1) 200-250 Other licensed brokers and/or I.D.A.C.) Canadian Stock Exchanges (non Members of Toronto, Montreal and

Total Bank of Canada Chartered Banks Members of the I.D.A.C.

185

8

1

194

CATEGORIES OF MEMBERS OF THE I.D.A.C. - BY SIZE OF AVERAGE QUARTERLY INVENTORY FOR 1961

- INCLUDING RELATED SALES VOLUME

TABLE 3

Average Quarterly Inventory	Federal Treasury Bills		Canadas & Guarantees Under 3 Years		Canada & Guarantees Over 3 Years		Provincial & Guarantees		Municipals, Schools & Hospitals		Corp. Bond & Deb. excluding Commercial Paper		TOTALS	
	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. Millions of \$'s	No. of Members	Combined Sales Vol. M Mln \$'s
\$														
0 - 24,999	168	36	133	99	128	186	133	107	139	44	119	94	65	187
25,000 - 99,999	-	-	14	30	20	97	19	25	22	46	38	85	35	138
100,000 - 499,999	3	44	11	109	23	344	19	265	18	111	19	327	44	310
500,000 - 999,999	-	-	9	178	6	259	5	171	4	77	2	47	8	161
1,000,000 - 4,999,999	3	460	8	652	8	1076	9	721	2	90	7	827	17	1067
Over 5,000,000	11	5602	10	3551	-	-	-	-	-	-	-	-	16	14066
TOTALS	185	6142	185	4619	185	1962	185	1289	185	368	185	1400	185	15929
											Less Commercial & Finance Co. Paper		149	
													15780	

Source: I.D.A.C. Survey of Members, 1962

REPORT OF THE BOARD OF DIRECTORS

FOR THE YEAR ENDING DECEMBER 31, 1900

1901

No.	Name	Age	Sex	Profession	Religion	Marital Status	Date of Birth	Date of Admission	Date of Discharge	Total Time in Service	Pay	Gratuities	Total Compensation	Remarks
1	John A. Smith	35	M	Engineer	Methodist	Married	1865	1885	1895	10	\$1,000.00	\$500.00	\$1,500.00	Discharged
2	James H. Jones	40	M	Teacher	Baptist	Single	1860	1880	1890	10	\$800.00	\$400.00	\$1,200.00	Discharged
3	William E. Brown	30	M	Farmer	Presbyterian	Married	1870	1890	1900	10	\$600.00	\$300.00	\$900.00	Discharged
4	Robert L. White	25	M	Student	Episcopal	Single	1875	1895	1900	5	\$400.00	\$200.00	\$600.00	Discharged
5	Charles F. Green	38	M	Merchant	Anglican	Married	1862	1882	1892	10	\$1,200.00	\$600.00	\$1,800.00	Discharged
6	Thomas G. Black	42	M	Physician	Methodist	Married	1858	1878	1888	10	\$1,500.00	\$750.00	\$2,250.00	Discharged
7	Edward D. Gray	28	M	Engineer	Baptist	Single	1872	1892	1900	8	\$700.00	\$350.00	\$1,050.00	Discharged
8	Franklin R. Hall	32	M	Teacher	Presbyterian	Married	1868	1888	1898	10	\$900.00	\$450.00	\$1,350.00	Discharged
9	George W. King	36	M	Farmer	Episcopal	Married	1864	1884	1894	10	\$850.00	\$425.00	\$1,275.00	Discharged
10	Henry J. Lee	40	M	Merchant	Anglican	Married	1860	1880	1890	10	\$1,100.00	\$550.00	\$1,650.00	Discharged
11	John C. Miller	34	M	Engineer	Methodist	Single	1866	1886	1896	10	\$1,050.00	\$525.00	\$1,575.00	Discharged
12	James B. Wilson	38	M	Teacher	Baptist	Married	1862	1882	1892	10	\$950.00	\$475.00	\$1,425.00	Discharged
13	William H. Moore	30	M	Farmer	Presbyterian	Married	1870	1890	1900	10	\$750.00	\$375.00	\$1,125.00	Discharged
14	Robert A. Taylor	26	M	Student	Episcopal	Single	1874	1894	1900	6	\$500.00	\$250.00	\$750.00	Discharged
15	Charles E. Evans	39	M	Merchant	Anglican	Married	1861	1881	1891	10	\$1,300.00	\$650.00	\$1,950.00	Discharged
16	Thomas H. Scott	41	M	Physician	Methodist	Married	1859	1879	1889	10	\$1,600.00	\$800.00	\$2,400.00	Discharged
17	Edward G. Adams	29	M	Engineer	Baptist	Single	1871	1891	1900	9	\$800.00	\$400.00	\$1,200.00	Discharged
18	Franklin S. Baker	33	M	Teacher	Presbyterian	Married	1867	1887	1897	10	\$920.00	\$460.00	\$1,380.00	Discharged
19	George H. Clark	37	M	Farmer	Episcopal	Married	1863	1883	1893	10	\$880.00	\$440.00	\$1,320.00	Discharged
20	Henry K. Lewis	43	M	Merchant	Anglican	Married	1857	1877	1887	10	\$1,400.00	\$700.00	\$2,100.00	Discharged

Co. 1st Regt. N.Y. Inf.

Report of the Board of Directors for the year ending December 31, 1900.

TABLE 4

THE INVESTMENT DEALERS' ASSOCIATION OF CANADA
SUMMARY OF REPORTS BY MEMBERS

SCHEDULE B

INVENTORY OF FIXED INCOME SECURITIES HELD BY MEMBERS

- Notes 1. This summary shows total inventory of fixed income securities held by Members during the calendar year 1961 on a quarterly basis.
2. Securities owned by firm and held outside of Canada are not included.
3. Unsold balances of new issues in primary distribution are not included.
4. Members' portions of joint accounts are included.
5. Inventory is shown in thousands of dollars.
6. Short positions are indicated by the letter (s) at left of figure.

Type of Security	33 Nat'l & other major positioning houses				Remaining houses				Total			
	Inventory (thousands of dollars)				Inventory (thousands of dollars)				Inventory (thousands of dollars)			
	March	June	September	December	March	June	Sept.	Dec.	March	June	Sept.	Dec.
	31, 1961	30, 1961	30, 1961	31, 1961	31, 1961	30, 1961	30, 1961	31, 1961	Average	1961	30, 1961	1961
	Average				Average							Average
Fed. Treas. Bills	(s)5,235	(s)11,894	(s)11,894	(s)4,282	(s)4,282	50			(s)5,235	(s)11,894	(s)11,894	(s)4,282
	103,703	155,299	144,839	171,764	143,900			100	38	103,753	155,299	171,864
												143,938
Cdas & Guar. of 3 yrs. or less	(s)1,148	(s)1,241	(s)1,241	(s)597	(s)597	(s)75			(s)19	(s)1,223(s)	1,241	(s)616
	117,396	97,460	171,800	117,888	126,136	2,787	3,488	2,141	2,868	120,183	100,517	175,288
												120,029
Cdas & Guar. over 3 yrs.	(s)1,877 (s)	368	(s)3,697	(s)4,979 (s)	2,729	(s)194	(s)224		(s)105 (s)	2,071 (s)	368 (s)	3,921 (s)
	20,816	27,050	23,583	21,506	23,236	4,877	5,123	2,280	3,756	25,693	32,173	26,320
												23,786
												26,992
Prov. & Guar.	(s)125	(s)184	(s)184	(s)76	(s)76	(s)9 (s)	15 (s)	5 (s)	18 (s)	12 (s)	9 (s)	140 (s)
	23,249	11,852	25,347	26,850	21,824	3,774	1,801	4,075	3,238	27,023	13,653	29,422
												30,154
												25,082
Municip., school & hospital debts.	7,616	8,726	4,504	6,774	6,905	(s)4 (s)	10	(s)45 (s)	15 (s)	15 (s)	4 (s)	10
						4,044	3,227	3,299	3,536	11,660	11,953	7,803
												10,347
												10,441
Corp. Bonds & Debs.	22,373	25,368	22,776	30,164	25,170	(s)3	3,921	3,299	(s)9 (s)	3	(s)3	(s)9 (s)
						3,076	4,059	3,921	3,684	25,449	29,427	26,697
												33,840
												28,854
Finance & Com- mercial Paper	2,455	10,343	9,347	31,274	13,355	425	472	630	518	2,880	10,815	9,977
												(s)3
												31,821
												13,873
Total	(s)7,112 (s)1,641	(s)17,016	(s)17,016	(s)4,979 (s)7,684	(s)7,684	(s)207 (s)	103 (s)	232 (s)	(s)154 (s)	7,319 (s)	11,744(s)	17,248 (s)
	297,608	336,098	402,196	406,220	360,526	19,033	17,739	18,150	17,638	316,641	353,837	420,346
												421,841
												378,164
No. of Members reporting	33											
Source: I.D.A.C. Survey of Members, 1962.	152											
	185											

A.390

UNITED STATES DEPARTMENT OF AGRICULTURE BUREAU OF PLANT INDUSTRY WASHINGTON, D. C.

PLANT INDUSTRY REPORT NO. 100

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positions occur.

15. Over the years the efforts of dealers to achieve a proper mechanism for the handling of business has resulted in a program of careful selection and training of trading personnel, development and application of equipment, substantial expenditure for these facilities and the continual refinement of regulations and ethical practices. Each dealer employs from 1 to 21 trading personnel whose activities are related directly or indirectly to virtually all other departments and employees in the organization. The Trading Department may well be regarded as the nerve centre of a dealer's operations since advice must be sought in this area before any transaction of a primary or secondary nature can be completed.

16. A widespread system of branch operations has been developed by many dealers in Canada and some have established offices in the United States, Great Britain and Europe. Vast networks of private wires, private telephones and various public services are utilized to maintain constant contact with markets both national and international. This system of communications permits pertinent information and market changes to be available nationally within minutes with the result that an investor almost anywhere in Canada may keep abreast of current developments. Adequate and equal service is available almost simultaneously from coast to coast, allowing the industry to draw upon the savings of the nation. Customarily business may be conducted each business day between 9 a.m. and 5 p.m. in



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1 each of the time zones. During these hours traders
2 are constantly in contact with other dealers to make
3 their requirements and offerings known. By this method
4 markets are made and matching transactions can be
5 arranged.

6 17. Actions taken by the people responsible
7 for making secondary bond markets result from their
8 varying interpretations of the information which is
9 available to them. Markets do not remain static for any
10 prolonged period, as investors are constantly on the
11 alert to anticipate changing conditions which may or may
12 not come to pass but serve to stimulate market activity.
13 In considering bond markets, price levels in themselves
14 are not, generally speaking, of as much significance as
15 the rate of return or yield to maturity. For this
16 reason, prices for all categories of bonds, with the
17 exception of those which carry special features, tend to
18 move in the same direction when changes occur. This
19 frequently results, when interest rates are tending
20 higher, to create an oversupply of securities in the
21 market. This oversupply situation is corrected only
22 when investors feel prices have been reduced to an
23 attractive level. Conversely, when interest rates appear
24 to be working lower, supply dries up until a level is
25 reached which appears in the minds of investors to
26 warrant some liquidation. This process of adjusting
27 yields to changing conditions is aided and moderated
28 by those dealers who are prepared to anticipate such
29 swings and to take positions for their own account. When
30 a dealer has taken positions in certain issues and orders



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1 to buy or sell as the case may be are not forthcoming,
2 he is frequently obliged to hedge his positions in other
3 issues. In this way a determined effort is made to
4 maintain stability. Dealers perform this function in
5 anticipation of overall profitability in this area of
6 their operations. Frequently, of course, losses are
7 sustained through poor judgment or other factors beyond
8 their control. The ability of dealers to hedge long
9 positions is restricted by the limited number of
10 financial institutions who make it a practice to lend
11 bonds at reasonable rates. If a larger number of
12 institutions would make bonds available at competitive
13 rates for this purpose, the functioning of the market
14 would be materially improved. Bank of Canada, Chartered
15 Banks and Trust Companies have the necessary facilities
16 to accommodate such borrowers. It is suggested that this
17 practice be broadened and that dealers include the
18 figures of such borrowings in their weekly report to the
19 I.D.A.C.

20 (b) Regulation of Secondary Markets

21 18. There is relatively little direct
22 legislative regulation of secondary bond markets when
23 compared, for example, to the regulation of new issues
24 and primary markets. That this area of trading in
25 securities has not attracted restrictive legislation is
26 indicative of the generally high level of integrity with
27 which the dealers have conducted their business.
28 Legislation has, however, been enacted which requires
29 brokers, dealers and salesmen to be licensed before
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(b) Regulation of Secondary Markets

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19. Over the years specific regulations concerning the trading of securities by members of the I.D.A.C. have been developed by the industry as are described in the Blue Book of the Investment Dealers' Association of Canada, Pages 426 to 434 inclusive. Failure to abide by the Regulations is subject to certain penalties as outlined in By-Law No. 8 of The Blue Book. In addition to the penalties for breach of the Regulations, the District and National Business Conduct Committees have broad powers to fine, suspend and/or expel any member (1) whose business conduct or practice is unbecoming a member or detrimental to the Association or (2) whose financial arrangements, associations or affiliations are objectionable.

20. In addition to the I.D.A.C. whose regulations govern trading by its members across the country, there are Bond Traders Associations in Toronto and Montreal. These Associations operate independently but in close conjunction with the I.D.A.C. and their Trading Regulations are now identical. The Chartered Banks do not hold membership in the I.D.A.C. but Trading Departments are members of the Bond Traders Association. Consequently, they conduct their business in accord with the I.D.A.C. Regulations. While members of the I.D.A.C. are customers of the Chartered Banks, the latter are also competitors in various areas of the bond business, raising a question of possible conflict of interest. Nevertheless, it is suggested that the Chartered Banks perform a useful service as participants in the secondary market. The Bond Traders Associations recommend changes

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1 in trading regulations to the I.D.A.C. as market
2 conditions dictate, and it is very rarely that these
3 suggestions are not acted upon by the senior body.

4 21. As evidence of the integrity of the
5 participants in the secondary market, it is interesting
6 to note that transactions customarily are made verbally,
7 with written confirmation being received the day
8 following that on which the business was done. It is
9 seldom that any misunderstanding has occurred, but when
10 this has happened between dealers, the Bond Traders
11 Associations and the I.D.A.C. have been able to settle
12 the matter quickly without reference to arbitration
13 outside the Associations.

14 (c) Capital and Margin Requirements

15 22. The capital requirements for membership in
16 the I.D.A.C. are stated in Appendix "A" of this I.D.A.C.
17 brief. For those dealers who undertake liabilities of
18 some consequence either for primary or secondary market
19 operations, the need is substantial. A schedule of
20 margin requirements, established to the satisfaction
21 of the banking system, affords adequate protection to
22 the lender for loans made to dealers against securities
23 pledged. In addition to these minimum stipulations
24 further specific liquid capital requirements must be
25 maintained. This program is supervised by an
26 established audit system and failure to comply is subject
27 to certain penalties. Specific details of capital and
28 margin requirements are contained in the I.D.A.C. Blue
29 Book, By-Law Number 8A, pages 334-338 and Regulations
30 pursuant thereto pages 405 to 412.

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(d) Characteristics

23. The character of the secondary market is conditioned by the supply and types of securities which are available for trading. The table following indicates the supply of Canadian debt securities as at December 31, 1961 by par value and the approximate number of individual issues.

TABLE 5

	<u>TOTAL DEBT (1) OF CANADA</u> <u>in millions of dollars</u>	<u>NO. OF</u> <u>ISSUES (2)</u>
Canada Treasury Bills	1,885	26
Canadas & Guarantees (ex savings bonds)	12,663	41
Provincials & Guarantees	8,190	700 ¹
Municipals	3,960	4000 ¹ (estimated)
Corporates	7,117	1000 ¹ (estimated)
TOTALS	33,815	5767

Source: (1) Bank of Canada, Personal Communication, April, 1962.

(2) Various personal communications.

24. While there is a yield relationship which prevails throughout most categories of bonds, the trading characteristics vary from one class to another. The secondary market for Treasury Bills and Canadas under 3 years to maturity (the "Money Market") are covered in Appendix G of this I.D.A.C. brief and will not be discussed herein.

25. The volume of trading in Canadas and Guarantees maturing beyond 3 years is normally greater

(7) Summary

23. The character of the secondary market is conditioned by the supply and types of securities which are available for trading. The table following indicates the supply of Canadian debt securities as at December 31, 1961 by par value and the approximate number of

Individual Issues

Table 1

in millions of dollars		TOTAL (1)
ISSUES (2)		
26	1,885	Canada Treasury Bills
41	12,663	(ex savings bonds)
700	8,190	Provincials & Guarantees
4000	3,960	Municipals
1000	7,117	Corporates
5767	33,815	TOTAL

Source: (1) Bank of Canada, Personal Communication, April, 1962.

(2) Various personal communications.

24. While there is a yield relationship which prevails throughout most categories of bonds, the trading characteristics vary from one class to another. The secondary market for Treasury Bills and Canadas under 3 years to maturity (the "Money Market") are covered in Appendix G of this I.D.A.C. brief and will not be discussed herein.

25. The volume of trading in Canadas and Guarantees maturing beyond 3 years is normally greater



1 than in categories other than Money Market. In the
2 earlier maturities of this group the market has
3 reasonable depth and resilience but breadth is confined
4 mainly to dealers, banks and other financial institutions.
5 At present the longer end of the Canada market cannot
6 be said to have normal depth, breadth or resilience.
7 Such depth as does exist is provided mainly by the
8 activities of the Securities Purchase Fund recently
9 established by the Government. Reasons for this
10 condition are dealt with in Section IV of this brief.

11 26. Provincial issues have good resilience
12 and depth since unhhibited factors of supply and demand
13 determine market levels. There is a steady flow of new
14 issues coming to market and at the same time Sinking Fund
15 operations combined with regular investment demand create
16 a relatively stable balance. Certain issues,
17 particularly those of Ontario and Quebec, can be said
18 to have breadth due to a broad public interest within
19 those Provinces but others appear to be restricted,
20 in the main, to an institutional market.

21 27. Municipal bonds are primarily sold in the
22 form of serial issues which tends to limit secondary
23 trading. Resale can be arranged, usually on an order
24 basis, through those dealers who participate actively
25 in the municipal market. In the few instances where term
26 bonds exist, a generally favourable market is available.

27 28. The market for Corporation bonds has
28 breadth and resilience. However, after the first flush
29 of activity which follows primary issues, supply usually
30 becomes difficult to obtain. If, in due course, some

than in categories other than Money Market. In the earlier maturities of this group the market has reasonable depth and resilience but breadth is confined mainly to dealers, banks and other financial institutions. At present the longer end of the Canada market cannot be said to have normal depth, breadth or resilience. Such depth as does exist is provided mainly by the activities of the Securities Purchase Fund recently established by the Government. Reasons for this condition are dealt with in Section IV of this brief. 26. Provincial issues have good resilience and depth since unhindered factors of supply and demand determine market levels. There is a steady flow of new issues coming to market and at the same time sinking fund operations combined with regular investment demand create a relatively stable balance. Certain issues, particularly those of Ontario and Quebec, can be said to have breadth due to a broad public interest within those Provinces but others appear to be restricted, in the main, to an institutional market.

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28. The market for Corporation bonds has breadth and resilience. However, after the first flush of activity which follows primary issues, supply usually becomes difficult to obtain. It, in due course, some



doubt is cast upon the credit of any issuer, a supply then becomes available and investment buyers are difficult to find until the situation is clarified. Such cases frequently produce a speculative interest resulting in active trading. Corporate bonds with special features, such as convertibility, warrants, etc., usually have an active market depending on the performance of the associated equity.

29. It is interesting to note that in most circumstances the spread between bid and asked prices is relatively narrow. For example, in categories ranging from Government of Canadas maturing beyond 3 years through Provincials and Municipals to Corporates, the spread between the bid and asked price customarily ranges from $1/8$ of 1 per cent to $1/2$ of 1 per cent in the more actively traded issues. This is brought about by keen competition among dealers and results in investors of all classes having access to fair prices. It is felt that the market as a whole has reasonable depth, but on some occasions investors wish to move actively in a similar direction, creating difficulty in maintaining a narrow price range. This is termed a "one-way market". In such instances, dealers who are prepared to take positions help to alleviate the situation until such time as investment buyers or sellers can be found.

IV. SOME FACTORS AFFECTING SECONDARY MARKETS

External

30. The relative levels at which bonds sell in the market are basically established by present, and estimates of future, supply of and demand for funds. As

doubt is cast upon the credit of any issuer, a supply then becomes available and investment buyers are difficult to find until the situation is clarified. Such cases frequently produce a speculative interest resulting in active trading. Corporate bonds with special features, such as convertibility, warrants, etc., usually have an active market depending on the performance of the associated equity.

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IV. THE MARKET FOR GOVERNMENT BONDS

30. The relative levels at which bonds sell

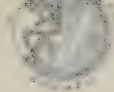
in the market are basically established by present, and estimates of future, supply of and demand for funds. As



1 Canada is a developing country, there has almost always
2 been a greater supply of bonds available than there have
3 been funds seeking investment. If, during the early
4 years of development, Great Britain, and in more recent
5 times the United States, had not supplied large amounts
6 of capital for the purchase of fixed-interest bearing
7 securities, our economy could not have expanded to the
8 degree which has been reached. Since we have had to
9 depend on imports of capital to supplement what we were
10 able to generate internally, our interest rate structure
11 originally followed the levels established in Great
12 Britain, but for many years now has been more closely
13 aligned to that prevailing in the United States. It is
14 only natural, therefore, that interest rates in Canada be
15 higher than those prevailing in the United States if
16 funds are to be attracted to this market from time to
17 time. While the trend of interest rates in Canada
18 usually adjusts to the general pattern in the United
19 States, following a reasonable interval, it does not seem
20 likely that any regular spread in rates between the two
21 markets can be established. This thesis is borne out by
22 reference to Charts I and II. Definition of a regular
23 spread would seem to be precluded as policies peculiar
24 to one or other of the two countries are varied,
25 producing changes in the attitude of investors.

26 Internal

27 31. With the influence of the American
28 interest rate structure in mind, there are many factors
29 of a purely Canadian nature which constantly have a
30 bearing on the level of prices in our bond market.

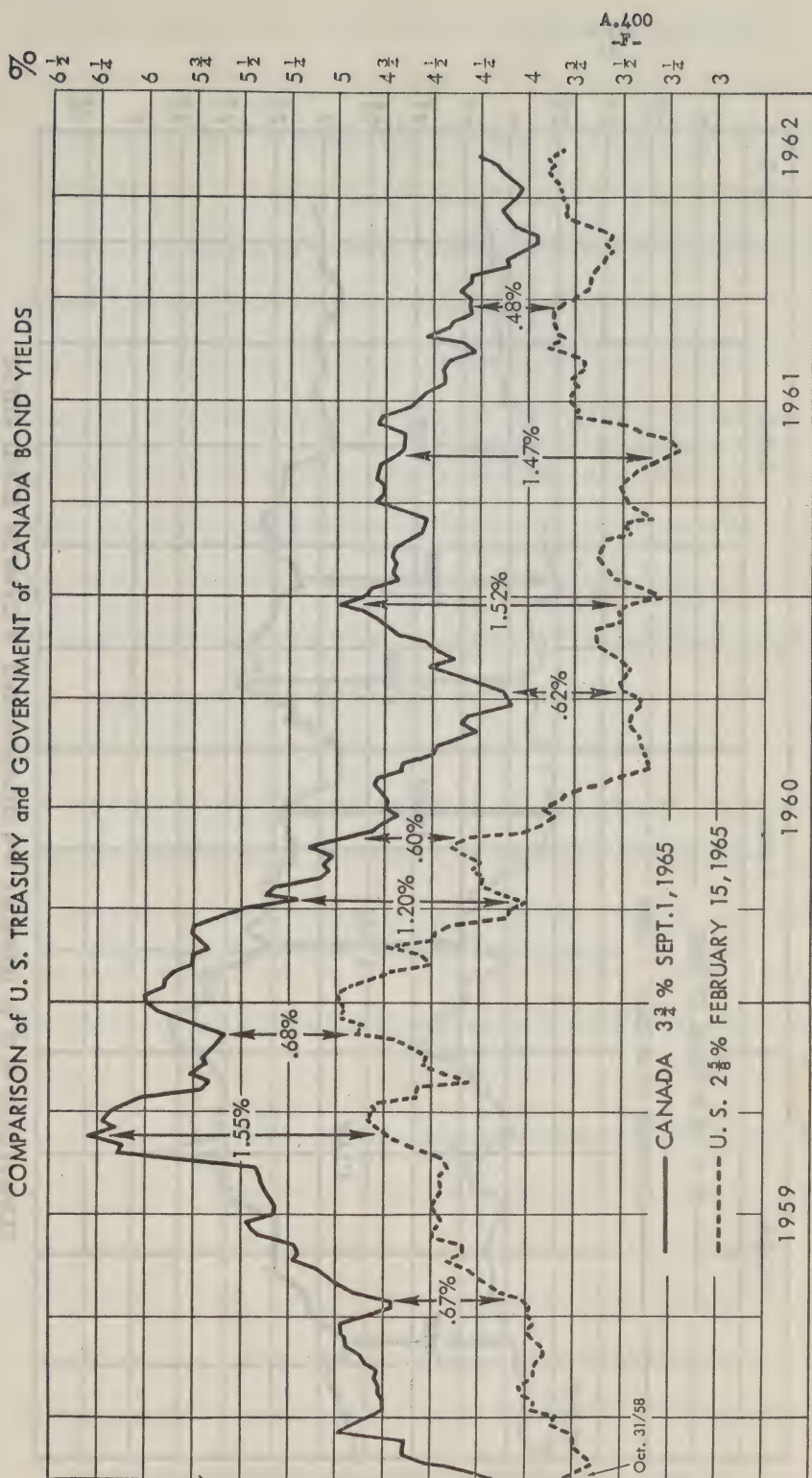


Canada is a developing country, there has almost always been a greater supply of bonds available than there have been funds seeking investment. If, during the early years of development, Great Britain, and in more recent times the United States, had not supplied large amounts of capital for the purchase of fixed-interest bearing securities, our economy could not have expanded to the degree which has been reached. Since we have had to depend on imports of capital to supplement what we were able to generate internally, our interest rate structure originally followed the levels established in Great Britain, but for many years now has been more closely aligned to that prevailing in the United States. It is only natural, therefore, that interest rates in Canada be higher than those prevailing in the United States if funds are to be attracted to this market from time to time. While the trend of interest rates in Canada usually adjusts to the general pattern in the United States, following a reasonable interval, it does not seem likely that any regular spread in rates between the two markets can be established. This thesis is borne out by reference to Charts I and II. Definition of a regular spread would seem to be precluded as policies peculiar to one or other of the two countries are wanted, producing changes in the attitude of investors.

Conclusion

31. With the influence of the American interest rate structure in mind, there are many factors of a purely Canadian nature which constantly have a bearing on the level of prices in our bond market.

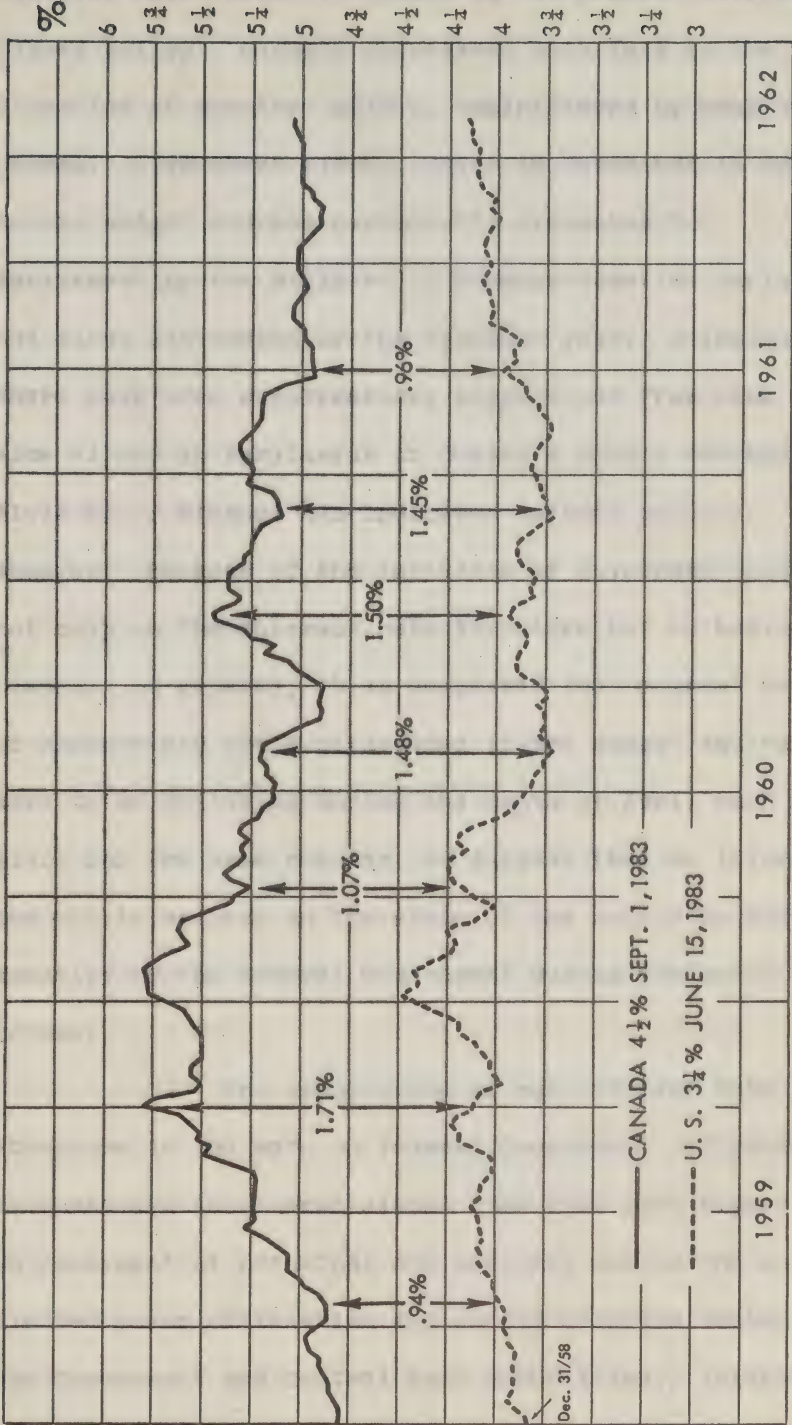
COMPARISON of U. S. TREASURY and GOVERNMENT of CANADA BOND YIELDS



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1 Probably the single most important factor relating to
2 interest rate trends in Canada is the Federal Government's
3 fiscal policy. Closely associated with this is the
4 direction of monetary policy, administered by Bank of
5 Canada. Government fiscal policy is described in the
6 annual budget address customarily presented to
7 Parliament by the Minister of Finance sometime during
8 the first six months of the calendar year. Occasionally
9 there have been supplementary budgets and from time to
10 time either in Parliament or during a public address the
11 Minister of Finance has indicated certain policy
12 changes. Because of the influence of Government policy,
13 not only on the interest rate structure but on business
14 planning in general, it is suggested that a great deal
15 of uncertainty would be avoided if the budget address
16 were to be delivered during the month of April each year.
17 Also, for the same reasons, we suggest that an informat-
18 ive public address on the state of the nation be made
19 annually by the Federal Government during the month of
20 October.

21 32. The cornerstone of our interest rate
22 structure is the rate on Federal Government obligations
23 as these are considered almost risk free with regard
24 to repayment of principal and interest due to the un-
25 limited power of taxation and credit creation vested in
26 the Government and Central Bank authorities. Interest
27 rates for Government of Canada Bonds are, therefore, the
28 prime rates on which rates for other bonds of similar
29 maturities are based and from which the others vary
30 according to the credit rating of the borrower.



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1 33. During periods of economic recession and
2 unemployment the practice of deficit financing for the
3 purpose of revitalizing the economy has been generally
4 accepted as a necessary social obligation. However,
5 during the past 7 fiscal years ending March 31st, (1955-
6 61 incl.) we have shown cash deficits in 6 years (with
7 a small surplus in 1957) and the certainty of a deficit
8 in the year ending March 31st, 1962. These deficits
9 have occurred despite periods of prosperity which
10 occurred during the years 1955-56, 1958-59 and 1961.
11 These factors, together with the concurrent increase in
12 money supply which has been necessary to finance the
13 deficits, have done a great deal to destroy the
14 confidence of investors in Government of Canada
15 securities. Stability of price, which was the prime
16 consideration in the minds of investors when they
17 purchased Government of Canada securities, has been
18 sharply reduced in this period. To take up the slack
19 in Government financial requirements during recent
20 years, the terms of the annual offering of Canada
21 Savings Bonds have been expanded to the extent that a
22 total amount in excess of 4 billion dollars is now held
23 by the Canadian public. It would appear that the
24 original intention of making this instrument available
25 to the small saver and the payroll savings group has
26 been discarded in favour of using the program as a means
27 of obtaining funds on a volume basis.

28 34. The investor has also been encouraged by
29 the 20 per cent dividend tax credit to become more
30 interested in equities which are regarded as some



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1 protection against inflationary tendencies. While this
2 has been beneficial to the financing of Canadian industry
3 through equity issues, with an increasing volume of
4 savings moving into the stock market, the private
5 investor would seldom find himself in a position of
6 wanting to purchase more than \$10,000 of Government of
7 Canada Bonds during the period of a year and this amount
8 he has recently been able to obtain in the form of
9 Canada Savings. These factors have tended substantially
10 to reduce the number of private investors as buyers of
11 Government bonds not carrying an early redemption
12 privilege. Additional features concerning the Canada
13 Savings program are discussed in Appendix B of this
14 I.D.A.C. brief and mention is made of them here only to
15 describe the influence which they have exerted on the
16 breadth of the market for Government securities. The
17 high level of taxation which has been reached, together
18 with the erosion which has occurred in the purchasing
19 power of our dollar, has tended to divert the interest
20 of most investors away from Government of Canada
21 securities and toward the higher yielding Provincial,
22 Municipal and Corporation bonds. At the same time, the
23 cost of capital to these more junior borrowers has been
24 increased.

25 35. The institutional investor who, for one
26 reason or another, must maintain a substantial portfolio
27 of longer term bonds has reduced proportionately his
28 holdings of Government of Canada Bonds and increased
29 the other three categories. In other words, the
30 professional investor regards those securities carrying

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1 additional yield as compensation for the loss of price
2 stability which was formerly provided by Government of
3 Canada securities.

4 36. Other investors such as the Chartered
5 Banks, Trust Companies, and Corporations are, however,
6 substantial buyers of short dated Government bonds.
7 Only in this area, can volume be obtained to meet their
8 requirements and, of course, prices are relatively stable
9 due to the nearness of maturity. This section of the
10 market has been greatly broadened and deepened due to
11 the development of the money market which was undertaken
12 in 1954. The particulars of this operation are
13 discussed in Appendix G of this I.D.A.C. brief.

14 37. The Federal Government recently has
15 followed a policy of obtaining its requirements, both
16 for new cash and refundings, from the short to medium
17 term areas of the market. This has helped to remove
18 pressure from the long term market and has made possible
19 financing by Provincial and Municipal Governments as
20 well as Corporate borrowers, many of whom would otherwise
21 have been obliged to borrow in the United States market.
22 In addition, the newly operating Securities Purchase Fund
23 and the retirement and cancellation of bonds held by the
24 Unemployment Insurance Fund, as announced in the Budget
25 of June/61, have helped to reduce the supply of long
26 term bonds for which there has been virtually no other
27 demand and consequently have helped to maintain
28 relatively stable market levels. While such programs
29 are of importance in providing temporary support to
30 bond markets, it would appear to be unrealistic to

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bond markets, it would appear to be unrealistic to



1 continue indefinitely a program of debt monetization.
2 Rates of interest on Government of Canada bonds set the
3 standard for most other classes of bonds. It is obvious
4 that a method to restore confidence in Federal
5 Government securities is of major importance if markets
6 are to be stabilized over the long-term and the general
7 functioning of the economy is to be improved.

8 38. There are many technical innovations which
9 might be introduced in an effort to re-establish
10 confidence in Government securities. However, it is
11 felt that most technical suggestions would probably tend
12 to veer away from orthodox financing practices and
13 would result in only artificial stability. The problem
14 should be approached through a program which will
15 improve the intrinsic value of Government bonds. It
16 would seem, therefore, that the major factors for
17 consideration would be:

18 1. A determined effort to hold
19 government spending within a balanced
20 budget during other than recessionary
21 periods and that when deficit spending
22 appears to be necessary, sincere effort
23 be made to direct funds toward the
24 areas which are most likely to produce
25 growth.

26 2. A re-examination of the tax structure
27 and a revision to an equitable level to
28 produce greater incentive and growth
29 without reducing revenues.

30 39. If the basic problem of lack of confidence

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39. If the basic problem of lack of confidence



1 could be satisfactorily resolved, the functions of the
2 secondary market would help to establish a stable
3 interest rate structure which would greatly benefit the
4 conduct of the economy.

5 40. Bank of Canada re-discount rate should
6 revert to a stated rate which would permit the
7 authorities to indicate clearly the intended direction
8 of monetary policy (see also Appendix "C"). This in turn
9 should permit greater flexibility by the Chartered Banks
10 in their administration of prime and call loan rates.
11 These rates appear to have been somewhat higher than
12 necessary during several protracted periods, which may
13 have been brought about in an effort to compensate for
14 the unrealistic limitation of 6 per cent during periods
15 of monetary stringency. Call loans are supported by
16 adequate collateral, providing prime credit for the
17 Banks. Lack of flexibility by the Banks has driven
18 borrowers to non-bank lenders thus narrowing the market
19 by permitting potential investors to escape liability
20 while employing their funds profitably. It is also
21 suggested that non-bank lenders may not always be
22 equipped to supervise these loans as effectively as
23 the Chartered Banks. Nor does this procedure permit the
24 monetary authorities and others to have proper knowledge
25 of borrowing activity.

26 41. Income tax rates and the income against
27 which the tax is assessed differ from one class of
28 investor to another, as is indicated in Table 6.

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41. Income tax rates and the income against which the tax is assessed differ from one class of investor to another, as is indicated in Table 6.



TABLE 6 Approximate Tax Rates

<u>Some Canadian Investors</u>	<u>Coupon %</u>	<u>Capital Appreciation %</u>
Chartered Banks	50-53	50-53
Trust Companies, capital account	50-53	nil
guaranteed account	50-53	50-53
Insurance Co.'s - Life, mutual	nil	nil
Life, shareholder-owned	50-53*	nil
General	50-53	nil
Pension Funds	nil	nil
Mutual Funds - mutual	23	nil
- growth	50-53	nil
Estates and Trusts	14-80	nil
Charitable, Religious & Fraternal Organizations	nil	nil
Individuals	0-80	nil
Non-financial Corporations	50-53	nil
Provincial & Municipal Governments	nil	nil

* on that part of income which is transferred to shareholders' equity. This amount is set actuarially.

These approximate tax rates may be modified by rulings of taxing authorities according to individual circumstances.

42. In order to maximize after-tax income, the requirements of one investor will vary from those of another in a different tax classification. For example, an individual in the higher tax brackets would



TABLE 6
Approximate Tax Rates

Some Canadian Investors	Coupon	Capital
		Appreciation &
Investment Income	10-53	50-53
Trust Income	50-53	nll
Dividend Income	50-53	50-53
Insurance Co.'s - Life, Mutual nll		nll
owned	50-53*	nll
General	50-53	nll
Pension Funds	nll	nll
Mutual Funds - mutual	53	nll
- growth	50-53	nll
Estates and Trusts	14-80	nll
Charitable, Religious & Fraternal Organizations	nll	nll
Individuals	0-80	nll
Non-Financial Corporations	50-53	nll
Provincial & Municipal Governments	nll	nll

* on that part of income which is transferred to shareholders' equity. This amount is set separately.

These approximate tax rates may be modified by rulings of taxing authorities according to individual circumstances.

For example, an individual in the higher tax brackets would be subject to a different tax classification. For the purpose of this document, the rates are given as approximate.



be more interested in a low interest bearing security selling at a discount from par than in a high interest bearing security selling at par or at a premium over par, since he pays no income tax on capital appreciation. Conversely, pension funds, which are not taxable as to either income or appreciation, would be interested in the highest yield whether from a large coupon or from a substantial discount. As many investors are in a position to benefit greatly from non-taxable capital appreciation, bonds selling at a discount normally are in demand and trade on a lower yield basis than do higher coupon bonds. However, despite the lower gross yield such discount bonds usually provide a higher after-tax yield. Specific examples of the foregoing generalizations are shown in Table 7.

TABLE 7

Examples of Gross and After-Tax Yields

- tax rate taken as 50 per cent on interest income.

Issuer	Coupon	Maturity	Price %	Gross Yield %	After-tax Yield %
Prov.of Ont.	3%	Oct.1977	80.25	4.80	3.10
Prov.of Ont.	6%	Nov.1979	106.75	5.36	2.52
Canada	3 $\frac{1}{4}$ %	June,1976	83.25	4.89	3.08
Canada	5 $\frac{1}{2}$ %	Oct,1975	103.25	5.17	2.47

43. Differences in the length of time to maturity play an important part in the requirements of various classifications of investors. Some, such as Banks, Trust Companies and most non-financial corporations, are generally interested in short term securities as a high degree of liquidity is required for most of

be more interested in a low interest bearing security selling at a discount from par than in a high interest bearing security selling at par or at a premium over par, since he pays no income tax on capital appreciation. Conversely, pension funds, which are not taxable as to either income or appreciation, would be interested in the highest yield whether from a large coupon or from a substantial discount. As many investors are in a position to benefit greatly from non-taxable capital appreciation, bonds selling at a discount normally are in demand and trade on a lower yield basis than do higher coupon bonds. However, despite the lower gross yield such discount bonds usually provide a higher after-tax yield. Specific examples of the foregoing generalization are shown in Table V.

TABLE V
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- tax rate taken as 50 per cent on interest income

	Price	Yield	Yield
		a	b
Prov. of Ont. 3½ Oct. 1977	80.25	4.50	3.10
Prov. of Ont. 6½ Nov. 1979	100.75	5.36	2.52
Canada 3½ June, 1976	83.25	4.89	3.06
Canada 3½ Jan. 1977	100.25	4.17	2.50

43. Differences in the length of time to

maturity play an important part in the negotiations of various classifications of investors. Some, such as Banks, Trust Companies and most non-financial corporations, are generally interested in short term securities as a high degree of liquidity is required for most of



1 their funds. Others are usually prepared to invest
2 in mid to long term securities although for particular
3 reasons, such as an anticipated decline in the market,
4 they may invest some of their funds in short term
5 securities.

6 44. Bond issues for which Sinking Funds or
7 Purchase Funds have been established normally have a
8 more favourable market than term bonds without these
9 provisions. The annual requirements of such funds,
10 affording underlying purchasing power in the market
11 coupled with consequent debt reduction prior to maturity,
12 creates broad investor confidence. Bonds issued with
13 stipulated instalments maturing each year over the term
14 of the obligation (serial bonds) are commonly sold to
15 investors who do not contemplate re-sale. As a result,
16 the secondary market for such bonds is not active
17 although, through negotiation, other purchasers can
18 usually be found. Bond issues which are sold by way of
19 private placement to a limited number of financial
20 institutions are not as a rule actively traded in the
21 secondary market. As in the case of serial bonds,
22 the investor purchases such issues with the intention of
23 holding until redemption. However, new investors can
24 usually be found should the original investor care to
25 liquidate his holding.

26 45. Bonds carrying special provisions, such
27 as convertibility into common stock, warrants to purchase
28 stock and/or a bonus of common shares, trade in the
29 secondary market at prices which bear greater relation
30 to the performance of the underlying equity than to the



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1 normal interest rate structure. Convertible bonds,
2 for the period of convertibility (which commonly is
3 less than the full maturity of the bond), usually
4 trade at a premium over the related value of the under-
5 lying equity. When the warrant or bonus features have
6 been detached, or when convertibility has expired or
7 lacks current value, the market for such bonds
8 develops in line with the normal interest rate structure,
9 having regard to the credit rating of the issuer.

10 V. RELATIONSHIP OF BANK OF CANADA TO SECONDARY MARKETS

11 46. Bank of Canada has Securities Represent-
12 atives situated in its offices in Toronto and Montreal
13 who maintain contact with the Investment Industry.
14 Transactions may normally be arranged through them for
15 the account of the Bank between the hours of 10:00 a.m.
16 and 3:30 p.m. Transactions on behalf of others for
17 whom they are acting may be arranged during the trading
18 hours of 9:00 a.m. and 5:00 p.m. When the Bank has
19 an interest in any specific issue either as principal or
20 agent, its policy is to consider firm offerings and
21 firm bids. Infrequently an immediate reply may be
22 forthcoming, but on most occasions approval must be
23 obtained from the main office of the Bank in Ottawa.
24 Delays of up to several hours are not uncommon causing
25 considerable uncertainty to the market. As Bank of Canada
26 is an important and generally active participant in
27 the secondary market, it is recommended that a program
28 of expediting reply be implemented.

29 47. Deleted.

30 48. Bank of Canada deals in securities to

2 for the period of convertibility (which commonly is

3 less than the full maturity of the bond), usually

4 trade at a premium over the related value of the under-

5 lying equity. When the warrant or bonus features have

6 been detached, or when convertibility has expired or

7 lacks current value, the market for such bonds

8 develops in line with the normal interest rate structure,

9 having regard to the credit rating of the issuer.

10 V. RELATIONSHIP OF BANK OF CANADA TO SECONDARY MARKETS

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15 the account of the Bank between the hours of 10:00 a.m.

16 and 3:30 p.m. Transactions on behalf of others for

17 whom they are acting may be arranged during the trading

18 hours as well.

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1 implement monetary policy, to adjust portfolio, to
2 act on behalf of Purchase Fund and Government accounts,
3 and more recently to redistribute certain new issues
4 which it has accepted in whole or in part at time of
5 issue. Consideration of methods used in distributing
6 new issues is presented in Appendix "B" of this I.D.C.A.
7 brief. However, the type of issue which is more or less
8 continuously available to investors ("a tap issue") is
9 harmful to the free operation of market forces as it
10 effectively establishes a ceiling on prices or may well
11 lead to overspeculation by dealers in their efforts to
12 fully purchase, i.e. "clean up" the total issue. The
13 market would function more effectively if substantial
14 portions of all such issues were offered to the public
15 at advertised prices and it is recommended that this
16 policy be followed in future.

17 49. Deleted.

18 50. There is doubt that the Central Bank
19 should act as agent for Government accounts and Purchase
20 Fund as this seems to centralize a disproportionately
21 large amount of the total funds which are actively in the
22 market. Such accounts might be handled by the Department
23 of Finance or by establishing separate trading functions
24 for each account, thus reducing possible conflict with
25 monetary policy.

26 51. It is recognized that many dealers and
27 others have become accustomed to the present operations
28 of the Bank and spend a great deal of time in trying to
29 anticipate the Bank's policy. Inevitably some of such
30 judgments prove to be incorrect and many have been prone



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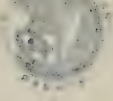


1 to find fault with the Bank for not following the
2 course which they had anticipated. If the above
3 suggestions were implemented such people would be obliged
4 to rely upon their own judgment and could not blame
5 the monetary authorities for their own errors.

6 VI. MARKET DATA, AVAILABILITY AND ADEQUACY

7 52. In the normal course of events there is
8 much statistical data which is regularly referred to in
9 assessing market behaviour. For example, the weekly
10 Financial Statistics provided by Bank of Canada enable
11 those interested to keep abreast of many important
12 factors. The Investment Dealers Association gathers and
13 makes available to its members statistics relating to
14 their overall non-bank loaning position. The Association
15 also provides the press with a regular service covering
16 the more actively traded issues. Individual dealers
17 supply the public with quotation sheets, money market
18 statistics, general market comment, specific bids and
19 offerings, and a flow of general information. The
20 Dominion Bureau of Statistics supplies much useful
21 statistical information. The Department of Trade and
22 Commerce publishes reports on the Outlook for Private
23 and Public Investment in Canada. In addition to
24 these sources of information which are readily available,
25 there are a number of statistical and/or forecasting
26 services available in Canada whose information and
27 projections are useful in predicting future yield trends.

28 53. Information relating to Central Bank action
29 in the market and the reasoning behind such action would
30 enable the market to function more smoothly. At present,



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1 the only detailed comment available on the Bank's
2 actions and objectives is contained in its Annual Report.
3 A regular report similar to the Monthly Review of the
4 Federal Reserve Bank of New York or the Quarterly Review
5 of the Bank of England would be helpful to market
6 participants.

7 VII. CONSIDERATION OF A BOND EXCHANGE

8 54. From time to time, the question has
9 arisen as to whether an organized Bond Exchange would
10 provide better operating results than are now available
11 through the dealer secondary bond market. There are
12 some aspects of an organized exchange which might be
13 beneficial but it is submitted that the present system,
14 which has evolved over the years, is best suited to meet
15 the requirements of bond trading.

16 55. Some of the advantages of an exchange
17 operation would appear to be the recording of volume and
18 price changes and establishment of a focal point which
19 might attract greater participation by the general public.
20 However, bond quotations are readily available and
21 volume figures would have little meaning since one major
22 transaction would far outweigh, in its influence, any
23 number of small transactions. The equity market is
24 representative of almost every type of private industry
25 and, while the market generally may be moving in one
26 direction, special considerations may cause some stocks
27 to move against the prevailing trend. This divergence
28 of trends is not a factor in bond markets, since in
29 most cases prices are based on yield. Individual
30 price changes are, therefore, not significant since



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1 arbitrage quickly adjusts discrepancies.

2 56. The level of bond yields is largely
3 developed by those professionals who manage substantial
4 portfolios. The price at which the small investor
5 may deal is, as a result, usually established by the
6 major investor and provides the former with the safeguard
7 of professional judgment. Furthermore, dealers who
8 position bonds usually complete such transactions at net
9 prices in line with institutional prices and consequently
10 the private individual completes his business at a
11 minimum of cost. If an organized bond exchange were
12 established to replace the over-the-counter market,
13 substantial costs for additional facilities would be
14 required. The added cost of these facilities would
15 have to be borne by the public in the form of established
16 commissions. As an example, a dealer would regard a
17 spread of 1/2 of 1 per cent, or \$50 on a \$10,000
18 corporation bond transaction in the secondary market, as
19 reasonable compensation. Under stock exchange
20 commission schedules, a \$10,000 transaction in shares
21 of the same company selling at \$50 would cost the
22 investor \$80.

23 57. An exchange-type transaction requires
24 the matching of off-setting orders with the broker acting
25 as agent. However, due to the size of many bond
26 transactions it would be unusual at any given time to
27 find that matching orders existed. In recognition of
28 this, dealers have organized themselves to assume
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1 bond market, the problem of investors moving in the
2 same general direction frequently presents difficulties
3 and these would be greatly aggravated by disclosure
4 of transactions on an organized exchange market.

5 58. Bonds are traded on the New York Stock
6 Exchange but only in relatively moderate volume. It is
7 noteworthy that in the report of the Joint Congressional
8 Committee's, "Study of the Dealer Market for Federal
9 Government Securities" (Washington, 1960), it is stated
10 that in 1958 only \$1.4 billion in bonds were traded on
11 the N.Y.S.E. vs. \$176 billion of sales of Federal
12 Government Securities alone through the dealer market.
13 The latter figure does not include corporate, state
14 and municipal bonds for which the volume of transactions
15 through the over-the-counter market is not available.
16 It is also notable that while bonds are traded through
17 the London Stock Exchange, volume and prices of trans-
18 actions are not published. Bonds, which formerly were
19 traded on the Montreal Stock Exchange, have not been
20 traded there for over 10 years and bond transactions
21 on the Toronto Stock Exchange in 1961 aggregated only
22 \$14,435,000 of which \$11,250,000 were Treasury Bills.
23 For comparison, the approximate total volume of bond
24 trading by members of the I.D.A.C. in the over-the-
25 counter market in Canada during 1961 was in excess of
26 15 3/5 billion (Ref. Table 1).

27 59. It would seem, therefore, that the
28 investing public in Canada can be best served at the
29 lowest cost by the present system. A similar
30 conclusion regarding the necessity of a dealer market



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27 \$2. It would seem, therefore, that the
28 investing public in Canada can be best served at the
29 lowest cost by the present system. A similar
30 conclusion regarding the necessity of a dealer market



for bonds has been reached in a study of the United States market. (Roosa, Robert V. - "Federal Reserve Operations in the Money and Government Securities Markets Federal Reserve Bank of New York 1956, page 34).

VIII RECOMMENDATIONS

<u>Reference</u>			This brief has pointed out the importance
<u>to Text</u>			of the secondary bond market to the
Para.	Page		capital market in particular and to the
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			bond market functions reasonably well
			under present conditions, it is suggested
			that certain changes can, and should be
			made which would improve its utility in
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			of the nation.
32	17	1.)	Yields on Government of Canada
			securities are the foundation of our
			interest rate structure. Recurring
33	17		deficits coupled with inflationary
			increases in the money supply and other
34	17 & 18		factors, have severely damaged the
			confidence of investors in Government
			securities and thus threaten the whole
35	18		market for fixed income bearing securities.
			To restore confidence in Government
			securities and stabilize the interest
37	18 & 19		rate structure it is strongly recommended
			that:
		(a)	a determined effort be made
			to balance the Federal Budget



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38 19 during other than recessionary
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(b) the nation's tax structure be
38 19 examined and revised in order
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and growth throughout the economy.

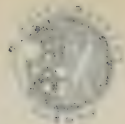
2.) The information presently available
52 24 to the secondary market is, for the main
part, adequate for investment decisions.

However, there are areas in which
31 14 & actions and policy of the Federal
17 Government are not clearly stated. It
is suggested that implementation of the
following recommendations would
materially aid dealers and investors
in assessing Government influences on
the secondary market and would assist
in re-establishing confidence in
Government securities.

(a) Deliver the Federal Budget
during the month of April
each year.

(b) Deliver an annual informative
public address on the state of
the nation during the month of
October.

3.) Bank of Canada, as agent for
Government accounts and as the administ-
rator of monetary policy, is one of the
most important factors in the secondary



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2			
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29			strator of monetary policy, is one of the
30			most important factors in the secondary



market. It is suggested that the following recommendations would improve the functioning of the secondary market and would assist the Government's and the Bank's direction of the economy.

(a) Bank of Canada re-discount rate

40 20 should revert to a stated rate thus indicating the direction of monetary policy.

(b) The Bank should implement a program designed to expedite reply to firm bids and offerings, thus removing one cause of uncertainty in the market.

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48 23
(c) "Tap issues", which are more or less continuously available to the market, are harmful to the free operation of market forces. Substantial portion of such issues should be offered to the public at advertised prices at the time of issue.

(d) In order to decentralize some of the funds in the market and to avoid possible conflicts with monetary policy, Government accounts and Purchase Fund should be handled by the Department of Finance or separate trading agencies.

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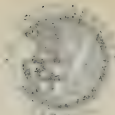
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Toronto, Ontario

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1 (e) A practice of issuing regular
2 quarterly reports by Bank of Canada,
3 similar to the Monthly Review of the
4 Federal Reserve Bank of New York or the
5 Quarterly Review of the Bank of England,
6 would aid the market's understanding of
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APPENDIX G

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Bank of Canada
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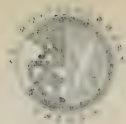
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SHORT-TERM MONEY MARKET BRIEF

I. FORMATION AND GROWTH

(1) The money market in Canada had its earliest beginnings in 1934 when 91-day Treasury Bills were first sold by tender. The number of issues increased progressively and by 1937, tenders were held every other week and in 1953 a weekly tender was introduced. During this period, the Chartered Banks were the principal buyers and only occasional trades took place between the banks and the Bank of Canada. The banks did not trade with each other. Investment dealers performed a very limited role at this time, but they occasionally tendered for Treasury Bills on behalf of clients or purchased bills from the banks against orders. During the early nineteen fifties, certain dealers carried modest amounts of Treasury Bills in inventory and this increased as the Bank of Canada at the same time increased its market spreads and allowed the dealers further scope for their operations.

(2) Early in 1954, the Bank of Canada agreed to give certain dealers limits or lines of credit by which Treasury Bills could be discounted at the Bank under a sales repurchase agreement. This privilege was made available at a lower interest rate than that charged by the Chartered Banks under their call loans in order to encourage the dealers to trade in bills and carry an inventory. The market began to develop quickly from this point and the eligible paper was expanded to short-term Government of Canada bonds and guarantees maturing within three years. Thirteen dealers received lines of



THE CANADIAN TREASURY BILL MARKET

1. INTRODUCTION

(1) The money market in Canada had its earliest beginnings in 1934 when 91-day Treasury Bills were first sold by tender. The number of issues increased progressively and by 1937, tenders were held every other week and in 1953 a weekly tender was introduced. During this period, the Chartered Banks were the principal buyers and only occasional trades took place between the banks and the Bank of Canada. The banks did not trade with each other. Investment dealers performed a very limited role at this time, but they occasionally tendered for Treasury Bills on behalf of clients or purchased bills from the banks against orders. During the early nineteen fifties, certain dealers carried modest amounts of Treasury Bills in inventory and this increased as the Bank of Canada at the same time increased its market spreads and allowed the dealers further scope for their operations.

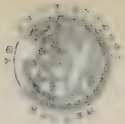
(2) Early in 1954, the Bank of Canada agreed to give certain dealers limits or lines of credit by which Treasury Bills could be discounted at the Bank under a sales repurchase agreement. This privilege was made available at a lower interest rate than that charged by the Chartered Banks under their call loans in order to encourage the dealers to trade in bills and carry an inventory. The market began to develop quickly from this point and the eligible paper was expanded to short-term Government of Canada bonds and guarantees maturing within three years. This market has since grown to



1 credit at the Bank of Canada and since that time the
2 number has varied between twelve and the present fourteen.
3 The names of the money market dealers, on March 31, 1962,
4 are given in Exhibit "A".

5 (3) The next important step occurred in June
6 1954 when the first day-to-day loans were made by the
7 Chartered Banks to the money market dealers. It was felt
8 that if the money market dealers were to carry substantial
9 inventories of bills and short governments, it was
10 necessary that they should be able to finance these
11 inventories at relatively attractive rates and low margin
12 requirements to create reasonable incentives. The
13 creation of the day loans provided the banks with a
14 highly liquid earnings asset and allowed them to make
15 the fullest possible use of other funds. The day loans
16 were designed so that they could be called by either
17 party prior to 12 o'clock on each business day. During
18 the first week, the day-loan rate was set at $1\frac{1}{2}$ per
19 cent, and thereafter the rate varied in response to
20 monetary conditions. As a further aid, the banks agreed
21 to communicate through an exchange broker the latest
22 rates established on any transaction to one million or
23 more. The Chartered Banks further co-operated by
24 reducing their overcertificates charge from $1/100$ of 1
25 per cent (\$100 per million) to $1/250$ of 1 per cent (\$40
26 per million).

27 (4) A significant change in the monetary
28 system accompanied the formation of the short-term
29 market. Through an amendment in the Bank Act, the banks
30 were required to hold a cash reserve of 8 per cent,



credit at the Bank of Canada and since that time the number has varied between twelve and the present fourteen. The names of the money market dealers, on March 31, 1952, are given in Exhibit "A".

(3) The next important step occurred in June 1954 when the first day-to-day loans were made by the Chartered Banks to the money market dealers. It was felt that if the money market dealers were to carry substantial inventories of bills and short government bonds, it was necessary that they should be able to finance these inventories at relatively attractive rates and low margin requirements to create reasonable incentives. The creation of the day loans provided the banks with a highly liquid earnings asset and allowed them to make the fullest possible use of other funds. The day loans were designed so that they could be called by either party prior to 12 o'clock on each business day. During the first week, the day-loan rate was set at $\frac{1}{2}$ per cent, and thereafter the rate varied in response to monetary conditions. As a further aid, the banks agreed to communicate through an exchange broker the latest rates established on any transaction to one million or more. The Chartered Banks further co-operated by reducing their overcertificates charge from 1/100 of 1 per cent (\$100 per million) to 1/250 of 1 per cent (\$40 per million).

(4) A significant change in the monetary system accompanied the formation of the short-term market. Through an amendment in the Bank Act, the banks were required to hold a cash reserve of 3 per cent,



1 whereas prior to this a 5 per cent reserve had been
2 mandatory, although in fact the banks had tended to hold
3 a 10 per cent reserve for liquidity purposes.
4 Consequently the foregoing adjustment immediately made
5 available approximately \$200 million of investible funds.
6 During this time, the Central Bank was carrying out an
7 easy-money policy and, therefore, the money market in
8 Canada developed quickly with the banks showing good
9 demand for money market securities. The dealers built
10 up an inventory and began to call active markets.

11 (5) In November and December 1955, the Bank of
12 Canada "urged" (Bank of Canada Annual Report 1955, page
13 16) the Chartered Banks to adopt a policy of maintaining
14 cash and secondary reserves equal to 15 per cent of
15 Canadian deposit liabilities. Secondary reserves at that
16 time were defined as comprising of Treasury Bills and
17 day-to-day loans. The banks were still required to
18 maintain 8 per cent of cash against deposit liabilities.
19 The banks accepted the suggestion of the Bank of Canada
20 and since May 31, 1956 have maintained secondary
21 reserves above their required amount. This agreement,
22 although somewhat restricting the Chartered Banks'
23 operations, has allowed the banks to make minor
24 adjustment to their cash position through the day-loan
25 market without having to buy or sell Treasury Bills.

26 (6) In 1957, the banks eliminated the over-
27 certification charges on money market transactions
28 relating to the day-to-day banking of short-term
29 securities. From that time on, it was possible for
30 dealers to move their inventory from one bank to another,



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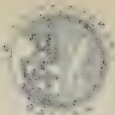


1 or to the Bank of Canada on a repurchase agreement,
2 without being penalized with an overcertification charge.
3 This was a further step to help the dealer broaden his
4 inventory position.

5 (7) The Bank of Canada added another facility
6 which greatly assisted the dealers in doing business
7 outside of Toronto and Montreal. This was an arrangement
8 whereby the Central Bank would release bonds at no cost
9 to the dealer at any one of the Bank's nine agencies
10 across the country; and after January 1957, any dealer
11 could hand in bills or short bonds at any agency of the
12 Bank of Canada, who would arrange to release the same
13 securities the same day at any other agency of the Bank.
14 Also during 1957, the use of Bank of Canada (same day)
15 funds were eliminated, except in relation to withdrawals
16 and deposits of currency and the making or repayment of
17 advances. All other transactions were settled in
18 clearing house (next day) funds. (Bank of Canada Annual
19 Report).

20 (8) Since 1954, the money market has expanded
21 greatly and the term "money market" now embraces many
22 transactions not related to Government of Canada short-
23 term obligations. The money-market dealers have actively
24 worked towards extending facilities of the market to
25 meet the requirements of both borrowers and lenders.
26 The various short-term obligations now in the money
27 market will be discussed in detail in this report.

28 (9) At the outset of the money market, the
29 dealer was a jobber owning an inventory of short-term
30 securities for stock-in-trade to service both his clients



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(7) The Bank of Canada added another facility which greatly assisted the dealers in doing business outside of Toronto and Montreal. This was an arrangement whereby the Central Bank would release bonds at no cost to the dealer at any one of the Bank's nine agencies across the country; and after January 1957, any dealer could hand in bills or short bonds at any agency of the Bank of Canada, who would arrange to release the same securities the same day at any other agency of the Bank. Also during 1957, the use of Bank of Canada (same day) funds were eliminated, except in relation to withdrawals and deposits of currency and the making or repayment of advances. All other transactions were settled in clearing house (next day) funds. (Bank of Canada Annual Report).

(8) Since 1954, the money market has expanded steadily and the Government of Canada short-term obligations not related to Government of Canada short-term obligations. The money-market dealers have actively worked towards extending facilities of the market to meet the requirements of both borrowers and lenders. The various short-term obligations now in the money market will be discussed in detail in this report.

(9) At the outset of the money market, the dealer was a jobber owning an inventory of short-term securities for stock-in-trade to service both his clients



1 and maintain an active trading market. Since dealer
2 inventory nearly always exceeds the capital of the firm,
3 it is necessary to borrow money to pay for the securities
4 by assigning the securities to the lender as collateral
5 for a loan. Initially most dealer loans were arranged
6 with the Chartered Banks; however, some repurchase or
7 buy-backs were arranged with investors as a convenient way
8 of providing the exact maturity date in cases where
9 Treasury Bills and other short-term obligations did not
10 have a suitable maturity date. The security used in
11 the repurchase agreement would normally be only slightly
12 longer than the term of the repurchase so that the
13 market liability of the dealer was kept to a minimum.
14 The repurchase agreements were, in effect, equivalent to
15 a security term loan and these transactions played a
16 considerable part in introducing non-bank corporate and
17 institutional investors to dealer loans. For short-term
18 investors, these secured loans to the dealers became
19 a convenient way of employing temporarily idle funds
20 without taking any market risk. The range of
21 collateral has broadened to include the obligations of
22 provinces, municipalities and corporations. The dealer
23 found that the ability to offer buy-backs to accounts
24 was often a valuable means of establishing business
25 contacts and, as a result, inventory was often carried
26 for the purpose of servicing these accounts. The role
27 of the dealers, therefore, began to resemble more closely
28 that of the London Discount Houses. The dealers took
29 on the role of loaning money to both governments and
30 corporations by owning their securities in inventory while

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1 borrowing funds from non-bank lenders to finance the
2 inventory. This aspect of the money market was described
3 in the Radcliffe Report. (Committee on the Working of
4 the Monetary System Report, page 58). "They earn their
5 living mainly by borrowing money more cheaply than they
6 lend it and, to some extent, from commissions and jobbing
7 profits. They borrow for shorter periods than the
8 periods of commitment in lending, (they 'lend short'
9 but borrow even 'shorter')....."

10 (10) The dealer, by owning securities to give
11 as collateral for repurchase loans as well as trading,
12 provides an active market in short-term securities
13 giving continuity and stability to the money market.
14 The study of the dealer market for federal government
15 securities, prepared by the Joint Economic Committee of
16 the Congress of the United States, (United States
17 Government Printing Office, Washington, 1960) states on
18 page 94 that "the growth of repurchase agreements during
19 the post-war years has played an important role in making
20 the money market more efficient. Through repurchase
21 agreements, the existence of higher interest rates is
22 brought to the attention of small banks and non-financial
23 corporations. Undoubtedly this has led to a more rapid
24 adjustment by the private economy to the effects of
25 changes in the supply of money and credit, and to a
26 reduction of the time lag between introduction of a
27 policy and the effectiveness of the policy". The dealer
28 fulfills the role of a banker inasmuch as temporarily
29 idle cash can be put to work for extremely short periods
30 of time. The question of statistics and controls of



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(10) The dealer, by making securities to give as collateral for repurchase loans as well as trading, provides an active market in short-term securities, giving continuity and stability to the money market. The study of the dealer market for Federal Government securities, prepared by the Joint Economic Committee of the Government Printing Office, Washington, 1950, states on page 94 that "the growth of repurchase agreements during the post-war years has played an important role in making the money market more efficient. Through repurchase agreements, the existence of higher interest rates is brought to the attention of small banks and non-financial corporations. Undoubtedly this has led to a more rapid adjustment by the private economy to the effects of changes in the supply of money and credit, and to a reduction of the time lag between introduction of a policy and the effectiveness of the policy". The dealer fulfills the role of a banker inasmuch as temporarily this cash can be put to work for extremely short periods of time. The question of statistics and controls of



1 dealer non-bank borrowing is discussed under the section
2 on "Country Banks."

3 II. INSTRUMENTS IN THE MARKET

4 (a) Government of Canada Treasury Bills

5 (11) Treasury Bills are currently offered weekly
6 by the Bank of Canada, acting on behalf of the Government,
7 through a competitive tender. There are no restrictions
8 on who may tender, but the Chartered Banks, money-market
9 dealers, and the Bank of Canada are the principal bidders.
10 Sealed tenders are submitted to the Bank of Canada and
11 are opened at 12 o'clock noon on Thursdays (except when
12 holidays intervene). The Treasury Bills are awarded
13 on the basis of price until the whole issue has been
14 allotted. Frequently a bidder will submit half a dozen
15 or more bids at different prices and only the highest
16 of these will be accepted. Generally the total bids
17 received from the banks and investment dealers, excluding
18 the Bank of Canada, are for a greater amount of bills
19 than those being offered so that all bids will not be
20 successful. The Bank of Canada will also bid in
21 competition with the others. It is the normal practice
22 for the Bank of Canada to submit a reserve bid for the
23 entire amount of each issue, in order to guard against a
24 situation in which the tenders of other bidders might
25 not be sufficient to subscribe for the entire issue.
26 (In England, "since the beginning of the Second World
27 War, it has been agreed by the discount houses who are
28 members of the London Discount Market Association that
29 the total of their bids will always cover the tender."
30 -Radcliffe Report, page 39 - Commercial banks do not



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tender directly for Treasury Bills in England). At approximately 2:00 p.m. on the day of the tender, each participant receives a telephone call from the Bank of Canada giving the following information:

(i) Number of bills won

(ii) High, low and average tender for each maturity offered

(iii) Total amount and maturity of bills to be tendered for on the following week.

(12) Since May 6, 1959, both 91-day and 182-day Treasury Bills have been offered. During the latter part of 1954 through November 1955, 273-day bills were offered. The following table shows the distribution of Treasury Bills as at December 31, 1961.

HOLDERS OF GOVERNMENT OF CANADA TREASURY
BILLS

(Detailed statistics as to the holders of Government of Canada Treasury Bills since 1954 will be found in Exhibit "B".)

(In \$000,000)

<u>As at December 31, 1961</u>	<u>Amount</u>	<u>%</u>
Bank of Canada	298	(16)
Chartered Banks	1,172	(62)
Government Accounts	8	(--)
General Public	<u>408</u>	<u>(22)</u>
TOTAL	1,886	(100)

(13) The statistics obtained by the Investment Dealers' Association indicate that members of the Association held an inventory of \$171,864,000 in Treasury Bills at 1961 year end, or 9.1 per cent of the Treasury Bills outstanding. As can be seen from the above table, the Chartered Banks are the principal owners of Treasury Bills and the main market for the dealer.



1000
1000

1000
1000

Under the terms of the Treasury Bill, the following information is given:

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HOLDERS OF GOVERNMENT OF CANADA TREASURY BILLS
(Detailed statistics as to the holders of Government of Canada Treasury Bills since 1954 will be found in Exhibit "B".)
(In \$000,000)

As at December 31, 1961	Amount	\$
Bank of Canada	298	(16)
Chartered Banks	1,175	(62)
Government Accounts	8	(--)
General Public	400	(22)
TOTAL	1,886	(100)

(13) The statistics obtained by the Investment Dealers' Association indicate that members of the Association held an inventory of \$171,864,000 in Treasury Bills at 1961 year end, or 9.1 per cent of the Treasury Bills outstanding. As can be seen from the above table, the Chartered Banks are the principal owners of Treasury Bills and the main market for the dealer.



1 The dealer, as mentioned earlier, will often carry
2 Treasury Bills as inventory so that repurchase
3 agreements can be entered into with particular accounts.

4 (14) The Chartered Banks tender for bills each
5 week for their own account and provide the principal
6 market for Treasury Bills in Canada. Inasmuch as they
7 have to compete at the tender, they do not always obtain
8 their full requirements and have to purchase bills in
9 the market. Dealers from time to time enter into pre-
10 tender contracts with the Chartered Banks, in which they
11 agree to confirm to the bank a stated amount of bills
12 at the average tender yield, less .02 per cent in basis.

13 (15) At certain periods in the past when
14 Canadian Treasury Bill yields were well above those
15 prevailing in other countries and the cost of foreign
16 exchange hedge was not prohibitive, bills were sold to
17 non-residents. The introduction of the 15 per cent
18 withholding tax on Treasury Bills, instituted on March
19 16, 1961, reduced the sale to non-residents substantially.
20 The withholding tax is calculated in such a manner as
21 to prove more discriminating to non-residents than a 15
22 per cent withholding tax would imply. (See Exhibit "C"
23 regarding calculation of withholding tax on Treasury
24 Bills.)

25 (b) Short-Term Government of Canada and
26 Government of Canada Guaranteed Bonds

27 (16) Unfortunately the Bank of Canada
28 statistics relating to the distribution of short-term
29 bonds only include those having a maturity of two years
30 and under. Therefore, complete statistical information

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relating to the accepted money market maturities of three years and under is not available. It will be a recommendation of this report that statistics regarding the outstanding amount and distribution of Government and Government guaranteed bonds, maturing within three years and under, be made available. The table below gives the distribution of Government securities maturing within two years as at December 31, 1961:

HOLDINGS OF GOVERNMENT OF CANADA BONDS
(See Exhibit "D" for holders of Government
of Canada bonds maturing two years and
under, from 1954 to 1961).

(OF A MATURITY TWO YEARS AND UNDER)

<u>As at December 31, 1961</u>	<u>Amount (\$'000,000)</u>	<u>%</u>
Bank of Canada	514	(16)
Chartered Banks	1,089	(34)
Government Accounts (est.)	60	(2)
General Public	<u>1,503</u>	<u>(48)</u>
TOTAL	<u>3.166</u>	<u>(100)</u>

(17) The Investment Dealers' Association statistics indicate that dealers held \$129,004,000 of short-term bonds, maturing within three years and under, in their inventory positions as of December 31, 1961. Information relating to holdings of the money-market dealers alone is not available.

(18) The long maturities issued by the Government (excluding C.N.R.) since the conversion loan of September 1, 1958 were all, with the exception of one issue, sold to the Bank of Canada for resale to the public. The long market has been relatively thin for government bonds, while the money market has grown rapidly so that funds appear to be available to satisfy most



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HOLDINGS OF GOVERNMENT OF CANADA BONDS
(See Exhibit "D" for holders of Government of Canada bonds maturing two years and under, from 1954 to 1961).
(ON A MATURITY TWO YEARS AND UNDER)

	Amount (\$'000,000)	As at December 31, 1961
Bank of Canada	514	(16)
Chartered Banks	1,059	(34)
Government Accounts (est.)	60	(2)
General Public	1,502	(48)
TOTAL	3,135	(100)

(17) The Investment Dealers' Association

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1 short-term borrowers at the present time. During the
2 past few years, the Government has been particularly
3 concerned about borrowing its cash requirements in the
4 short-end of the market, as can be illustrated by the
5 Minister of Finance's statement in the Budget of April
6 10, 1962:

7 "In my Budget speech last June,
8 I said that in order to avoid congestion
9 in the long market, we would for at least
10 several months confine new federal issues
11 to short-term bonds. During the past
12 nine months, we have issued no long-term
13 bonds; 375 million ranging in term from
14 $5\frac{1}{4}$ to 6 years were placed directly with
15 the Bank of Canada, and the terms of all
16 other market issues in no case exceeded
17 $3\frac{1}{2}$ years."

18 (19) One factor which should be mentioned
19 regarding the question of financing the short-term debt
20 of the federal government is that of competing for
21 corporate surplus funds. Corporations, being subject to
22 both federal and provincial taxes, are most attracted
23 to securities offering the highest net or after-tax
24 yield. Therefore, a low-coupon and high-discount bond,
25 which will have a certain portion of tax-free capital
26 appreciation, is relatively attractive. There has been
27 a strong incentive by borrowers to issue low-coupon,
28 deep-discount securities in the past. However, the
29 Budget of December 20, 1960, imposed the following
30 restrictions:



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I said that in order to avoid congestion in the long market, we would for at least several months continue to issue long-term

to short-term bonds. During the past nine months, we have issued no long-term bonds; 375 million ranging in term from 2½ to 6 years were placed directly with the Bank of Canada, and the terms of all other market issues in no case exceeded 3½ years."

(19) One factor which should be mentioned regarding the question of financing the short-term debt of the federal government is that of competing for corporate surplus funds. Corporations, being subject to both federal and provincial taxes, are most attracted to securities offering the highest net or after-tax yield. Therefore, a low-coupon and high-discount bond which will have a certain portion of tax-free capital appreciation, is relatively attractive. There has been a strong incentive by borrowers to issue low-coupon, deep-discount securities in the past. However, the Budget of December 20, 1960, imposed the following restrictions:



1 "that where the contractual rate
2 of interest on any bond, debenture, or
3 similar evidence of indebtedness, issued
4 by a tax-exempt borrower, is less than
5 5 per cent, and where the bond or
6 debenture is issued at a discount
7 which provides an effective yield to
8 maturity or to the earliest call date
9 that exceeds the contractual rate by
10 more than one-third, the whole discount
11 shall be deemed to be income in the
12 hand of the first Canadian resident
13 taxable holder of the instrument."

14 (See page 1011 Hansard, December 20,
15 1960.)

16 Prior to this legislation, coupons of as low as $1\frac{1}{2}$ per
17 cent were used by all levels of Government and
18 corporations alike in raising funds in the short-term
19 market.

20 (20) An exception to this practice of raising
21 money on low-coupon notes was the introduction, in the
22 issue of October 1, 1959, of \$250 million Government
23 of Canada $5\frac{1}{2}$ per cent, October 1, 1962, convertible
24 at the holder's option at any time prior to June 30,
25 1962, into $5\frac{1}{2}$'s October 1, 1975. This issue attracted
26 considerable attention from both corporate and
27 institutional investors. Since that time, an additional
28 \$100 million, $5\frac{1}{2}$ per cent of October 1, 1962, were
29 offered and \$448 million $5\frac{1}{2}$'s, April 1, 1963, convertible
30 into $5\frac{1}{2}$'s, due April 1, 1976.



"that where the contractual rate of interest on any bond, debenture, or similar evidence of indebtedness, issued by a tax-exempt borrower, is less than 5 per cent, and where the bond or debenture is issued at a discount which provides an effective yield to maturity on to the earliest call date that exceeds the contractual rate by more than one-third, the whole discount shall be deemed to be income in the hand of the first Canadian resident taxable holder of the instrument." (See page 1011 Hansard, December 20, 1960.)

Prior to this legislation, coupons of as low as 1/2 per cent were used by all levels of Government and corporations alike in raising funds in the short-term market.

(50) An exception to this practice of raising money on low-coupon notes was the introduction, in the issue of October 1, 1952, of \$250 million Government of Canada 5 1/2 per cent, October 1, 1962, convertible at the holder's option at any time prior to June 30, 1962, into 5 1/2's October 1, 1975. This issue attracted considerable attention from both corporate and institutional investors. Since that time, an additional \$100 million, 5 1/2 per cent of October 1, 1962, were offered and \$448 million 5 1/2's, April 1, 1963, convertible into 5 1/2's, due April 1, 1976.



(21) There are no restrictions on the investment dealers that can trade in the market in either Treasury Bills or short Government bonds. The various bond traders associations have established regulations relating to trading, which set the minimum size of trading at \$100,000, in order to provide a flexible and responsive market. The trading rules relating to the money market sector, laid down by the Toronto Bond Dealers' Association, are given in Exhibit "E".

(c) Bankers Acceptances

(22) Preliminary work has been done by both the Chartered Banks and money-market dealers, in conjunction with the Bank of Canada, in examining the possibility of an Acceptance market in Canada. The banks must initiate this new development by being prepared to "accept" corporate paper for a set fee. It is expected that the money-market dealers would be able to bank such paper in the day-loan market provided by the Chartered Banks and that it would, at some point, be eligible for rediscounting at the Bank of Canada. The dealer would be a jobber on such Acceptances and it is thought that the banks would be the principal buyers of the paper. Acceptances, as they are presently visualized, would provide the investor with a rate of return somewhat between Treasury Bills and prime finance paper. At the present time, certain questions of taxation have held up the introduction of Acceptances.

(d) Provincial and Municipal

(23) 1) Provincial - The provinces have been attracted to the short-term market to meet some of their

(21) There are no restrictions on the invest-

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(d) Provincial and Municipal

(23) i) Provincial - The provinces have been

attracted to the short-term market to meet some of their



1 requirements for funds. Although they have been
2 traditionally borrowers in the long-term market, they
3 have found that the developing short term money market
4 can provide them with a flexible source of funds to help
5 meet their total requirements. The money market has
6 provided them with a means of selling provincial
7 Treasury Bills (Manitoba and Saskatchewan), short-term
8 low-coupon bonds for periods of usually two years or
9 less, and parity bonds. Parity bonds compete for short-
10 term funds when the rates are attractive and when no
11 restrictions are placed on the amount sold to any one
12 purchaser.

13 (24) D.B.S. statistics provide some information
14 with regard to provincial short-term debt outstanding
15 and issued during the fiscal year, but this does not
16 include securities issued by authorities and guaranteed
17 by the provinces. Both British Columbia and Alberta
18 have been very active in financing some of their
19 requirements through provincial-guaranteed short-term
20 securities.

21 (25) The dealer syndicates formed to under-
22 write the long-term borrowing needs of the provinces
23 usually do not prohibit the dealer from negotiating
24 directly with the provinces for securities of two years
25 and under. Therefore, a considerable amount of short-
26 term financing by the provinces has been arranged
27 privately and little information is available. However,
28 some provinces, notably Alberta and British Columbia,
29 have called for tenders on particular blocks of short-
30 term maturities and dealers, in this case, will either



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term maturities and dealers, in this case, will either



1 tender alone or form a group to tender on a particular
2 offering.

3 (26) The majority of provincial short-term
4 bonds are offered as low-coupon as possible, under the
5 restrictions described on page A.433, paragraph 19.
6 Short-term provincial bonds do not trade actively.
7 Therefore, the owner of such investments, having to value
8 them on a regular basis, will usually receive a
9 theoretical valuation which is not subject to swings in
10 the market.

11 (27) 11) Municipal - A number of
12 municipalities, including such names as Metro Toronto,
13 cities of Toronto, Montreal, Hamilton, Winnipeg, Vancouver,
14 London, Kitchener and Kingston, have already taken
15 advantage of the short-term money market. Most
16 municipal borrowings are designed to meet current
17 expenditures prior to tax receipts being received, and
18 often allows them to choose the most favourable time for
19 financing in the long market.

20 (28) The larger municipalities call for tenders
21 on their short-term obligations; however, some are
22 arranged on a negotiated basis. Inasmuch as most
23 municipal short-term borrowings are relatively small,
24 dealers act independently and are not normally
25 restricted by syndicates when tendering for short-term
26 offerings.

27 (29) Little information is available to
28 indicate the amount of municipal short-term debt
29 arranged during the past few years. However, it
30 would appear that during the first quarter of 1962 in



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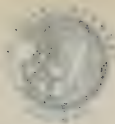
1 excess of \$35,000,000 was borrowed by municipalities in
2 the short term market.

3 (e) Finance Company Paper

4 Sales finance companies raise a substantial
5 percentage of their borrowing requirements in the money
6 market. Prime finance companies, including such names
7 as General Motors Acceptance Corporation, Industrial
8 Acceptance Corporation, Limited, Traders Finance
9 Corporation, etc., borrow for terms of one year or less
10 at somewhat similar rates. These rates are sensitive
11 to the supply and demand of short-term money and are
12 usually accurate indications as to the availability of
13 such funds. Second-line finance companies will pay rates
14 often up to 1/2 of 1 per cent more in order to meet their
15 borrowing requirements.

16 (31) The amount of finance paper outstanding
17 at the present time might be estimated to be in excess
18 of \$500 million. (The Federal Council of Sales Finance
19 Companies estimate that the ten largest finance
20 companies had short-term obligations during 1961 of
21 between \$410 million and \$525 million.)

22 (32) Dealers act as agents on behalf of the
23 finance companies and receive a commission for locating
24 purchasers of this paper. At certain times, dealers
25 will inventory this paper, but by doing so must find
26 suitable "country bank" accommodations to carry it.
27 I.D.A. statistics indicate that dealers were carrying
28 inventory of \$31 million in finance company and corporate
29 paper on December 31, 1961.
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4-7 Finance Companies

Sales finance companies raise a substantial percentage of their borrowing requirements in the money market. Prime finance companies, including such names as General Motors Acceptance Corporation, Industrial Acceptance Corporation, Limited, Western Finance Corporation, etc., borrow for terms of one year or less at somewhat similar rates. These rates are sensitive to the supply and demand of short-term money and are usually accurate indications as to the availability of such funds. Second-line finance companies will pay rates often up to 1 1/2 or 1 per cent more in order to meet their borrowing requirements.

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1 (f) Corporate Paper

2 (33) This sector of the money market has
3 attracted considerable attention inasmuch as it has
4 grown very rapidly and is a development that was not
5 visualized in 1954. Corporate paper has shown this
6 growth for several reasons. The cost of corporate
7 borrowings from the Chartered Banks has been relatively
8 high compared with the availability of short-term money,
9 and the corporate paper, itself, has found a ready market
10 with short-term investors. This is largely true because
11 corporations do not establish fixed rates at which they
12 will sell their paper and each is perfectly free to
13 choose whatever term or rate they think is necessary to
14 attract money. Therefore, the senior credits can compete
15 actively with finance companies through small variations
16 in rates paid. Corporate paper is also issued on a
17 "demand" basis by which the investor purchases a liquid
18 investment at a fixed rate of return. This paper can
19 be called on 24-hour notice by the purchaser, or in some
20 cases by both parties, and has become very attractive
21 to investors at times when the immediate outlook for
22 short-term rates is uncertain. The corporation borrowing
23 through "demand" paper also receives the advantage of
24 obtaining funds at the lowest possible rate. The return
25 on "demand" paper is closely related to the day-to-day
26 money rate and the 30-day prime finance paper rate.

27 (34) Corporate borrowers in the money market
28 include retail stores, oil companies, grain merchants,
29 chemical manufacturers, breweries, distillers, and many
30 others. These companies have been attracted to the money



(7) Corporate Paper

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(34) Corporate borrowers in the money market include retail stores, manufacturers, wholesalers, and many others. These companies have been attracted to the money



1 market primarily due to the relatively high cost of
2 borrowing at the Chartered Banks at the prime rate.
3 Exhibit "F" illustrates the spread between the prime
4 rate and the cost of 3-day money for a senior corporation
5 paper since 1959.

6 (35) It is expected that companies using the
7 money market for a certain part of their borrowing
8 requirements will have bank lines of credit available
9 to cover any amount of paper outstanding and, in most
10 cases, companies continue to borrow a certain amount
11 from their banks.

12 (36) Like many segments of the money market,
13 there is little or no statistical information available.
14 A survey of the larger borrowers as to their authorizat-
15 ion to borrow in the short-term market indicates that,
16 at any one time, there could be up to \$450 million
17 corporate paper in the market. However it is more
18 likely that the actual borrowings by corporations would
19 range between \$275 million and \$325 million at present.

20 (37) As the money market grows, there are
21 an increasing number of corporations of many kinds
22 borrowing in the short-term market, and it becomes more
23 difficult for the purchaser of the paper to be selective
24 and have time to examine the credit standing of each
25 name. It is important that, if the paper market is
26 to grow in a responsible manner, the buyers be fully
27 aware of the credits they are purchasing. This is
28 especially true as a large volume of paper is sold on a
29 "demand" basis and perhaps not enough attention is paid
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(38) The dealer normally acts as an agent in selling corporate paper and receives a smaller commission than that paid by finance companies. Although the commissions are small, the dealer often feels that establishing contact with the corporation to offer short-term paper can, in the long run, be most rewarding.

(g) Deposits

(39) 1) Chartered Banks - The banks recently established set rates at which they will accept deposits for terms of up to one year. These rates have tended to be 1/4 of 1 per cent below those offered by the prime finance companies but, on some occasions, the rates have competed with finance company paper. These deposits are often particularly attractive to those restricted to trustee investments. One bank issues deposit certificates for terms of one to six years at a published rate. These certificates can be transferred and have some measure of liquidity. The bank pays dealers a commission for placing these medium term certificates.

(40) The banks will also accept deposits in U.S. dollars at their American agencies. The Canadian banks compete among themselves for U.S. dollar deposits and do not keep to any uniform rate schedule. The banks are not restricted by regulations of the Federal Reserve Board as to the rate that may be paid on deposits of one year and under in the United States and, as a result, the Canadian banks have attracted a large number of deposits from both American institutions and corporations. The banks will also compete, between



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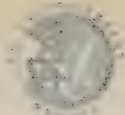


1 themselves, for U.S. dollar deposits from Canadians by
2 offering a Canadian account a U.S. dollar deposit fully
3 hedged. In this way, a Canadian account can purchase
4 U.S. dollars and leave them on deposit with a Canadian
5 bank in New York and sell the U.S. dollars forward at
6 maturity of the deposit, often obtaining a return in
7 excess of that paid by the finance companies in Canada.
8 U.S. dollar deposits with the Canadian banks in New
9 York are not subject to withholding tax.

10 11) Trust Companies

11 (41) Trust companies issue deposit receipts
12 which are non-transferable. Some provincial accounts,
13 municipalities and corporations, restricted to trustee
14 investments place their short-term funds with the trust
15 companies on deposit.

16 (42) The dealers play a considerable role in
17 helping the trust companies obtain deposits, and in
18 some cases the trust companies will pay a commission
19 for deposits obtained at a specified rate. However,
20 it is more usual for the trust company to accept a
21 deposit if a suitable offset investment can be arranged.
22 This involves the dealer originally locating the client,
23 agreeing on a rate at which the trust company deposit
24 would be attractive, then offering the trust company
25 an offset investment (finance or corporate paper, etc.)
26 at $1/4$ to $1/2$ of 1 per cent higher than the deposit
27 rate. Some trust companies pool all their short-term
28 investments in a central fund and accept deposits at
29 rates based on their over-all short-term earnings. Since
30 the banks have become more aggressive in seeking



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1 deposits, the trust companies too have had to become
2 more competitive, and it appears that they are becoming
3 more active in soliciting deposits rather than just
4 accepting them.

5 (h) Export Finance Corporation of Canada Limited

6 (43) Another recent issuer of short-term paper
7 is the Export Finance Corporation of Canada Limited,
8 which is wholly owned by Canada's eight Chartered Banks.
9 This corporation borrows money in the short-term market
10 in order to assist mid-term (one to five years)
11 financing for exports which have been insured by the
12 Export Credits Insurance Corporation, a Crown company.
13 Most of the notes which have been sold by the Export
14 Finance Corporation of Canada Limited have been payable
15 in U.S. dollars for periods up to 180 days, and have
16 been bought by the Chartered Banks directly from the
17 Corporation. However, dealers have placed \$16 million
18 with clients other than the Chartered Banks as of March
19 31, 1962. Short-term U.S. pay paper of Export
20 Finance Corporation is subject to a 15 per cent with-
21 holding tax.

22 III. PARTICIPANTS

23 (a) Bank of Canada

24 (44) 1) Dealer Lines of Credit - Money-market
25 dealers, as mentioned earlier, have lines of credit
26 with the Central Bank which allow them to enter into
27 repurchase agreements with the Bank to finance their
28 inventory of Treasury Bills and Government of Canada
29 money-market securities when other sources of
30 accommodation are not available. Thus, the Bank of



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(h) Export Finance Corporation of Canada Limited

(43) Another recent issuer of short-term paper is the Export Finance Corporation of Canada Limited, which is wholly owned by Canada's eight Chartered Banks. This corporation borrows money in the short-term market in order to assist mid-term (one to five years) financing for exports which have been insured by the Export Credits Insurance Corporation, a Crown company. Most of the notes which have been sold by the Export Finance Corporation of Canada Limited have been payable in U.S. dollars for periods up to 180 days, and have been bought by the Chartered Banks directly from the Corporation. However, dealers have placed \$10 million with clients other than the Chartered Banks as of March 31, 1962. Short-term U.S. pay paper of Export Finance Corporation is subject to a 15 per cent withholding tax.

III. FINANCIAL INSTITUTIONS

(a) Bank of Canada

(44) 1) Dealer Lines of Credit - Money-market

dealers, as mentioned earlier, have lines of credit with the Central Bank which allow them to enter into repurchase agreements with the Bank to finance their inventory of Treasury Bills and Government of Canada money-market securities when other sources of accommodation are not available. Thus, the Bank of



1 Canada is the "lender of last resort" for the dealer.
2 These lines are confirmed monthly and are open to some
3 negotiation. However, extensions to the existing
4 lines are usually granted for short periods when
5 requested. It is important for the development of the
6 money market that these lines be as flexible as possible
7 if the money market is to grow and adapt itself to
8 changing circumstances. The lines of credit, however,
9 must be related to the financial responsibility of
10 the money-market firm.

11 (45) ii) Bank Rate - There has been much
12 criticism directed at the variable Bank Rate since its
13 introduction on November 1, 1956. Elsewhere in the
14 I.D.A. brief, there is an expression of opinion that a
15 floating Bank Rate, calculated weekly at a rate of 1/4
16 of 1 per cent above the average price tendered for 91-day
17 Treasury Bills, gives little guidance to the market as
18 to the Bank of Canada and Government policy. However,
19 it is the feeling of this committee that the variable
20 Bank Rate is an important development in adapting the
21 Canadian money market to our particular monetary system.

22 (46) Dealer inventories of money-market
23 securities are normally financed through day-to-day loans
24 at the Chartered Banks, and these day loans form the
25 banks' most liquid asset next to cash. Therefore,
26 when the Central Bank adjusts the cash in the banking
27 system or a dislocation of cash between the eight banks
28 takes place, the availability of day loans can vary
29 greatly. Money-market dealers have been able to use
30 their lines of credit at the Central Bank during these



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1 periods of cash adjustment when day-to-day money is
2 not sufficient to look after their commitments in the
3 normal course of business. Dealers, knowing that the
4 Central Bank's reserves are available at a small penalty
5 rate, are, therefore, more active participants in the
6 money market. In this way, they can operate with
7 confidence knowing their position is always protected,
8 although they may have to pay the current Bank Rate
9 as established each week by the Bank of Canada.

10 (47) However, should the Bank of Canada
11 return to a traditional Bank Rate, then, because of the
12 dependency of the money-market dealers upon the "lender
13 of last resort" periodically, there should be an
14 additional flexible rate similar to the floating Bank
15 Rate so that money-market dealers could continue to
16 operate and be protected by their lines of credit at a
17 borrowing rate which is related to the current yields on
18 Treasury Bills. This rate might be renamed "Bank
19 Lending Rate" or "Bank Accommodation Rate."

20 (48) Dealers rediscounted securities, under
21 the purchase and resale agreement with the Bank of
22 Canada during 12 weeks of 1959, 17 weeks in 1960,
23 and 11 weeks in 1961, according to the weekly statistics
24 provided by the Bank of Canada.

25 111) Market

26 (49) The prime function of a mature money
27 market is to equate supply and demand of short-term
28 capital; the speed and flexibility of the market is
29 of the utmost importance. The dealers or "jobbers"
30 provide a market which is very sensitive as to price and



not sufficient to look after their commitments in the normal course of business. Dealers, knowing that the Central Bank's reserves are available at a small penalty rate, are, therefore, more active participants in the market. In this way, they can operate with confidence knowing their position is always protected, although they may have to pay the current Bank Rate as established each week by the Bank of Canada.

(17) However, should the Bank of Canada return to a traditional Bank Rate, then, because of the dependency of the money-market dealers upon the "lender of last resort" periodically, there should be an additional flexible rate similar to the floating Bank Rate so that money-market dealers could continue to operate and be protected by their lines of credit at a borrowing rate which is related to the current yields on bank deposits. This rate might be renamed "Bank Lending Rate" or "Bank Accommodation Rate."

the purchase and resale agreement with the Bank of Canada during 12 weeks of 1980, 17 weeks in 1981, and 11 weeks in 1982, according to the weekly statistics provided by the Bank of Canada.

(11) Market

(12) The prime function of a money market is to ensure supply and demand of short-term capital; the speed and flexibility of the market is of the utmost importance. The dealers or "jobbers" provide a market which is very sensitive as to price and



1 they transfer large amounts of securities with little
2 market dislocation. The problem of having two financial
3 centres in both Toronto and Montreal has been effectively
4 eliminated. However, the Bank of Canada's trading
5 departments in Toronto and Montreal, which are the
6 Bank of Canada's contacts with the market, lack
7 sufficient equipment and staff to handle the practical
8 problems relating to the money market. The dealer at
9 present finds it difficult to contact the Bank of
10 Canada quickly and receive immediate answers.

11 (50) The main criticisms concerning the
12 trading operations of the Bank are:

13 (a) Decisions concerning most transactions
14 are made in Ottawa and the Bank trader
15 is usually given little or no
16 discretionary powers.

17 (b) The Bank traders do not have direct
18 "key" telephone lines to money-
19 market dealers and Chartered Banks.

20 (c) One trader handles all sections of
21 the Government market and does not have
22 time to be fully acquainted with the
23 factors influencing the money market.

24 (51) (iv) Statistical Information - The Bank
25 of Canada publishes an excellent weekly and monthly
26 series of statistics, as well as an annual summary,
27 covering the Bank's, Federal Government's and Chartered
28 Banks' operations. These figures are of particular
29 interest to the money market because of information
30 relating to the cash position of the banking system as



they transfer large amounts of securities with little market allocation. The problem of having two financial centres in both Toronto and Montreal has been effectively eliminated. However, the Bank of Canada's trading departments in Toronto and Montreal, which are the Bank of Canada's contacts with the market, lack sufficient equipment and staff to handle the practical problems relating to the money market. The dealer at present finds it difficult to contact the Bank of Canada quickly and receive immediate answers.

(50) The main criticisms concerning the

trading operations of the Bank are:

(a) Decisions concerning most transactions

are made in Ottawa and the Bank trader

is usually given little or no

discretionary power.

(b) The Bank traders do not have direct

"key" telephone lines to money-

market dealers and chartered banks.

(c) One trader handles all sections of

the Government market and does not have

time to be fully acquainted with the

factors influencing the money market.

(51) Bank of Canada - The Bank

of Canada publishes an excellent weekly and monthly

series of statistics, as well as an annual summary,

covering the Bank's, Federal Government's and Chartered

Banks' operations. These figures are of particular

interest to the money market because of information

relating to the cash position of the banking system as



1 a whole and weekly changes in holdings of Government
2 securities, as well as weekly changes in Chartered
3 Bank loans (day-to-day loans, call loans, general loans,
4 etc.). However, statistics relating to the holding
5 of Government money-market securities, three years and
6 under, are not available, inasmuch as the official
7 breakdown of holdings of Government bonds is into
8 categories of two years and under and two years to five
9 years. It is suggested that the published statistics
10 should agree with the "market" definition of short-term
11 maturities, i.e. three years and under.

12 (52) At the present time, there is very little
13 information collected and published by the Bank of Canada
14 or D.B.S. relating to the new short-term issues of
15 provincial and municipal authorities, finance companies
16 and corporations. Inasmuch as this sector of the
17 money market is expanding rapidly, there should be a
18 better understanding of the role of each borrower.

19 (53) v) Loan of Securities - The Bank of
20 Canada at one time was prepared to enter into a
21 "reversible switch" arrangement for 30 days against
22 suitable collateral. However, the rates charged
23 appeared to be more than the market would bear and
24 little use was made of this facility.

25 IV. "Country Banks"

26 (54) The reasons for the development of
27 "country banking" is given in Section I. of this report.
28 As mentioned previously, the dealer is holding inventory
29 to "bank" out for short periods of time, is following
30 in the tradition of the twelve London discount houses



a whole and weekly changes in holdings of Government securities, as well as weekly changes in chartered Bank loans (day-to-day loans, call loans, general loans, etc.). However, massive changes in the holdings of Government money-market securities, three years and under, are not available, inasmuch as the official breakdown of holdings of Government bonds is into categories of two years and under and two years to five years. It is suggested that the published statistics should agree with the "market" definition of short-term maturities, i.e. three years and under.

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(53) v) Loan of Securities - The Bank of

Canada at one time was prepared to enter into a "reversible switch" arrangement for 30 days against suitable collateral. However, the rates charged appeared to be more than the market would bear and little use was made of this facility.

iv) "Country Banks"

(54) The reasons for the development of "country banking" is given in Section I. of this report. As mentioned previously, the dealer is holding inventory to "bank" out for short periods of time, as following in the tradition of the twelve London discount houses



1 and the seven American Government Bond dealers. (See
2 Pages A.427 and A.428, paragraphs 9 and 10.)

3 (55) The Investment Dealers Association, being
4 fully aware of the increasing use of non-bank borrowing
5 by the dealers, began last year to collect weekly
6 statistics relating to the current volume of securities
7 being financed through the "country banks". Each dealer
8 reports directly to the I.D.A. auditors once a week
9 the amount of Treasury Bills, money-market bonds,
10 Government of Canada's three years and under, and other
11 bonds banked away from the Chartered Banks. The combined
12 totals of these figures are made available to members
13 of the I.D.A., the Department of Finance, and the Bank
14 of Canada. On December 27, 1961, dealers were banking
15 out the following securities:

16 Securities Banked by Members of the I.D.A.
17 with the "Country Banks".

	(\$'000,000)
18 Treasury Bills	72.4
19 Money Market	17.1
20 Canada's (three years and over)	9.7
21 Other Securities (not including stocks)	<u>69.1</u>
22 TOTAL	<u>168.3</u>

24 (56) In 1961, there were 11 weeks during which
25 dealers banked over \$100 million in Treasury Bills away
26 from the banking system. Therefore, it can be seen that
27 the "country banks" helped finance a considerable portion
28 of the dealer inventories.



and the seven American Government Bond dealers. (See
 Pages A.427 and A.428, paragraphs 9 and 10.)
 (55) The Investment Dealers Association, being
 fully aware of the increasing use of non-bank borrowing
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 statistics relating to the current volume of securities
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 totals of these figures are made available to members
 of the I.D.A., the Department of Finance, and the Bank
 of Canada. On December 27, 1961, dealers were banking
 out the following securities:

Securities Banked by Members of the I.D.A.
 with the "Country Banks".

Treasury Bills	72.4
Money Market	17.1
Canada's (three years and over)	9.7
Other securities (not including above)	56.1
TOTAL	155.3

(\$100,000)

(56) In 1961, there were 11 weeks during which
 dealers banked over \$100 million in Treasury Bills away
 from the banking system. Therefore, it can be seen that
 the "country banks" helped finance a considerable portion
 of the dealer inventories.

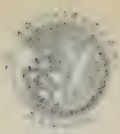


V. NON-RESIDENT SHORT-TERM INVESTMENTS
IN CANADIAN SHORT-TERM SECURITIES

(57) Non-residents have been active purchasers of Canadian short-term obligations over the past few years. Inasmuch as the Canadian dollar is not "pegged" and liable to wide swings, non-residents have been fully hedging their investments to eliminate any foreign exchange risk. It is usually possible to obtain forward exchange contracts for periods of up to one year. The fully hedged rate (the non-resident purchases Canadian dollars spot and sells forward at the maturity date of his investment) is dependent upon the cost or profit of hedging funds as well as the gross yield on the short-term obligation purchased.

(58) Prior to the introduction of the 15 per cent withholding tax on Treasury Bills, a considerable amount of Treasury Bills was sold abroad. Since that time, however, finance company and corporate paper has replaced Treasury Bills. This paper is also subject to a 15 per cent withholding tax deducted at maturity, but this tax is calculated and deducted easier than on Treasury Bills. In some cases, this resulted in the non-resident investor being introduced to alternative short-term investments in Canada that offered higher yields than those available on Treasury Bills. It should be remembered that short-term Government of Canada bonds, issued prior to December 20, 1960, are free of withholding tax to non-resident purchases.

(59) Short-term foreign flows of funds into Canada's money market on a fully hedged basis would



INVESTMENT IN CANADIAN SHORT-TERM DEBT

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of Canadian short-term obligations over the past few years. Inasmuch as the Canadian dollar is not "pegged" and liable to wide swings, non-residents have been fully hedging their investments to eliminate any foreign exchange risk. It is possible to hedge forward exchange contracts for periods of up to one year. The fully hedged rate (the non-resident purchases Canadian dollars spot and sells forward at the maturity date of his investment) is dependent upon the cost or profit of hedging funds as well as the gross yield on the short-term obligation purchased.

(58) Prior to the introduction of the 15 per

cent withholding tax on Treasury Bills, a considerable amount of Treasury Bills was sold abroad. Since that time, however, Treasury Bills have been replaced Treasury Bills. This paper is also subject to a 15 per cent withholding tax deducted at maturity, but this tax is calculated and deducted earlier than on Treasury Bills. In some cases, this resulted in the non-resident investor being introduced to alternative short-term investments in Canada that offered higher yields than those available on Treasury Bills. It should be remembered that short-term Government of Canada bonds, issued prior to December 20, 1960, are free of withholding tax to non-resident purchasers.

(59) Short-term foreign flows of funds into

Canada's money market on a fully hedged basis would



1 appear to have little influence on the factors
2 affecting non-resident control of Canadian resources
3 and manufacturing and, therefore, should not be subject
4 to strong discrimination. However, the amount of
5 non-resident ownership of money-market securities
6 should be known in case restrictions are placed by
7 foreign governments on their subjects investing funds
8 outside their borders. At present, it is doubtful if
9 any accurate figure of Canadian short-term paper owned
10 by non-residents is known but an estimate of 300 -
11 350 million dollars might be made. This figure would
12 include Treasury Bills, Government of Canada bonds,
13 finance and corporate paper.

14 (60) Canadian banks from time to time actively
15 solicit U.S. dollar deposits as described in the section
16 on bank deposits. The rate of return accruing to the
17 investor on these deposits is not subject to withholding
18 tax.

19 (61) Canadian short-term investors will also
20 place funds outside the country when foreign rates are
21 attractive. Most investments of this sort are also
22 made on a fully hedged basis. From time to time, the
23 hedged rate of return on U.S. Treasury Bills or short-
24 term paper becomes attractive largely due to the
25 profit that can be made on hedging the investment.
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REPORT OF THE COMMISSIONER OF THE TREASURY

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to strong discrimination. However, the amount of

non-resident control is not known.

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include Treasury Bills, Government of Canada bonds,

finance and corporate paper.

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solicit U.S. dollar deposits as described in the section

on bank deposits. The rate of return accruing to the

investor on these deposits is not subject to withholding

tax.

(61) Canadian short-term investors will also

invest in U.S. dollar deposits and in U.S. government

securities. Most investments of this sort are also

made on a fully hedged basis. From time to time, the

hedged rate of return on U.S. Treasury Bills or short-

term paper becomes attractive largely due to the

profit that can be made on hedging the investment.



RECOMMENDATIONS

References

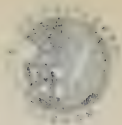
- 1) The money market performs an important function in contributing to Canada's economic development by helping to fully utilize all available sources of capital. It is, therefore, recommended that the money market should continue to receive the excellent support that it has obtained in the past from both the Bank of Canada and the Chartered Banks.

See Growth
of Money
Market.

- 2) The difficulty of obtaining accurate statistics for the preparation of a study on the money market illustrates the difficulty in assessing the roles of the various borrowers in the money market. It is recommended that more information be obtained and published concerning the borrowing by provinces, municipalities and corporations in the money market.

<u>Page</u> <u>No.</u>	<u>Para.</u> <u>No.</u>
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6	16
9	24
10	29
12	36
16	49



Kansas City, Mo.
January 1934

RECOMMENDATIONS

1) The money market performs an important function in contributing to the economic growth of the country by helping to fully utilize all available sources of capital. It is, therefore, recommended that the money market should continue to receive the excellent support that it has obtained in the past from both the Bank of Kansas and the Federal Reserve Bank of Kansas City.

See Growth
of Money

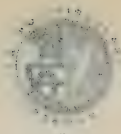
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2) The difficulty of obtaining accurate statistics for the preparation of a study on the money market illustrates the difficulty in assessing the roles of the various borrowers in the money market. It is recommended that more information be obtained and published concerning the money market. Therefore, municipalities and corporations in the money market.

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43 16



- 1 3) Short-term foreign flows of 18 57
2 funds into Canada's money market
3 on a fully hedged basis would
4 appear to have little influence
5 on the factors affecting non-
6 resident control of Canadian
7 resources and manufacturing
8 and, therefore, should not be
9 discriminated against. The
10 question of withholding tax on
11 all short-term investments
12 should be closely examined.
- 13 4) It is a recommendation that closer
14 liaison be established between the
15 Bank of Canada and the money- 15 49
16 market dealers for the purpose
17 of trading in money-market 16 50
18 securities.
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2
3 on a fully hedged basis would
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EXHIBIT "A"

MONEY MARKET DEALERS RECEIVING LINES OF CREDIT
AT THE BANK OF CANADA,
AS AT MARCH 31, 1962.

Ames, A.E., & Co. Limited

Burns Bros. & Denton Limited

Dominion Securities Corp. Limited

Equitable Securities Canada Limited

Gairdner & Company Limited

Greenshields & Company Inc.

Harris & Partners Limited

McLeod, Young, Weir & Co. Limited

Midland Securities Corp. Limited

Mills, Spence & Company Limited

Nesbitt, Thomson & Company Limited

Richardson, James, & Sons

Royal Securities Corp. Limited

Wood, Gundy & Company Limited



EXHIBIT "A"

MONEY MARKET DEALERS RECEIVING LINES OF CREDIT
AT THE BANK OF CANADA
AS AT MARCH 31, 1962.

- Ames, A.E., & Co. Limited
- Burns Bros. & Denton Limited
- Edwards Securities Canada Limited
- Gairdner & Company Limited
- Greenhalgh & Company Inc.
- Harris & Partners Limited
- McLeod, Young, Weir & Co. Limited
- Mills, Spence & Company Limited
- Richardson, James, & Sons
- Wood, Gundy & Company Limited

EXHIBIT "B"

HOLDERS OF GOVERNMENT OF CANADA TREASURY BILLS.

	(In \$000,000)															
<u>As at December 31st</u>	<u>1954</u>	<u>(%)</u>	<u>1955</u>	<u>(%)</u>	<u>1956</u>	<u>(%)</u>	<u>1957</u>	<u>(%)</u>	<u>1958</u>	<u>(%)</u>	<u>1959</u>	<u>(%)</u>	<u>1960</u>	<u>(%)</u>	<u>1961</u>	<u>(%)</u>
Bank of Canada	169	(22)	264	(22)	507	(32)	469	(29)	36	(2)	309	(15)	407	(20)	298	(16)
Chartered Banks	363	(46)	430	(35)	743	(47)	808	(50)	956	(64)	983	(48)	974	(49)	1172	(62)
Gov. Accounts	41	(5)	36	(3)	40	(3)	59	(4)	89	(6)	30	(1)	56	(2)	8	(--)
General Public	208	(27)	494	(40)	285	(18)	289	(17)	415	(28)	755	(36)	549	(29)	408	(22)
TOTAL	781	(100)	1,224	(100)	1,575	(100)	1,625	(100)	1,496	(100)	2,077	(100)	1,986	(100)	1,886	(100)

100



EXHIBIT "C"

WITHHOLDING TAX ON TREASURY BILLS

An extract from House of Commons Debates,
Vol. 105, No. 69, Official Report for Thursday, March
16th, 1961, page 3060, referring to an amendment to
Section 108 of Bill C-73.

"This amendment provides that when
a resident of Canada sells a Treasury
Bill to a non-resident, the non-resident
shall be deemed to have received a payment
of interest. The amount of interest he
shall be deemed to have received shall
be equal to the proportion of the
difference between the original issue
price and the face value of the bill,
that is, the proportion of the original
discount, which is attributable to the
unexpired portion of the term of the
bill remaining at the time it is
purchased by the non-resident.

"Since this amendment deems interest
to have been paid to the non-resident at
the time the non-resident purchased a
Treasury Bill, the Canadian resident
who sells the Treasury Bill will be
obliged to withhold the 15 per cent
non-resident withholding tax on the
amount that is deemed to be interest.

"If, at some subsequent time
before maturity, the non-resident sells



WITHHOLDING TAX ON TREASURY BILLS

An extract from House of Commons Debates,
Vol. 105, No. 69, Official Report for Thursday, March
16th, 1961, page 3060, referring to an amendment to
Section 103 of Bill C-73.

"This amendment provides that when

a resident of Canada sells a Treasury

~~bill to a non-resident, the capital~~

shall be deemed to have received a payment

of interest. The amount of interest he

shall be deemed to have received shall

be equal to the proportion of the

difference between the original issue

price and the face value of the bill,

that is, the proportion of the original

discount, which is attributable to the

unexpired portion of the term of the

bill remaining at the time it is

purchased by the non-resident.

"Since this amendment deems interest

to have been paid to the non-resident at

the time the non-resident purchased a

Treasury Bill, the Canadian resident

who sells the Treasury Bill will be

obliged to withhold the 15 per cent

non-resident withholding tax on the

amount that is deemed to be interest.

"If, at some subsequent time

before maturity, the non-resident sells



Nethercut & Young

Toronto, Ontario

A.456

- G -

1 the Treasury Bill back to a
2 Canadian resident, the non-resident
3 will be eligible for a refund of that
4 part of the tax he has paid which
5 is attributable to the unexpired portion
6 of the term of the bill."
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Canadian resident, the non-resident
will be eligible for a refund of that
part of the tax he has paid which
is attributable to the unexpired portion
of the term of the bill."

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EXHIBIT "D"

HOLDINGS OF GOVERNMENT OF CANADA BONDS

(OF A MATURITY TWO YEARS AND UNDER)

<u>As at December 31st</u>	<u>(In \$000,000)</u>													
	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>(%)</u>	<u>1957</u>	<u>(%)</u>	<u>1958</u>	<u>(%)</u>	<u>1959</u>	<u>(%)</u>	<u>1960</u>	<u>(%)</u>	<u>1961</u>	<u>(%)</u>
Bank of Canada	1,193	1,021	520*	(24)	779	(31)	245	(11)	514	(18)	353	(16)	514	(16)
Chartered Banks	636	475	406	(19)	410*	(16)	826	(36)	657	(23)	615	(28)	1,089	(34)
Gov. Accounts (est.)	N.A.	N.A.	165	(7)	126	(5)	243	(10)	86	(3)	111	(5)	60	(2)
General Public	<u>481</u>	<u>677</u>	<u>1,079</u>	<u>(50)</u>	<u>1,223</u>	<u>(48)</u>	<u>1,010</u>	<u>(43)</u>	<u>1,610</u>	<u>(56)</u>	<u>1,147</u>	<u>(51)</u>	<u>1,503</u>	<u>(48)</u>
TOTAL	<u>N.A.</u>	<u>N.A.</u>	<u>2,170</u>	<u>(100)</u>	<u>2,538</u>	<u>(100)</u>	<u>2,324</u>	<u>(100)</u>	<u>2,867</u>	<u>(100)</u>	<u>2,226</u>	<u>(100)</u>	<u>3,166</u>	<u>(100)</u>

*Owing to changes in valuation procedures, these figures are not comparable with those of the foregoing year.

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EXHIBIT "E"

TRADING REGULATIONS -- JANUARY 1, 1961

All transactions by dealers, whether acting in the capacity of either principal or agent, shall be as follows:-

- 2) There are no spread restrictions regarding trading of Government of Canada Bonds and Government of Canada Guaranteed Bonds having an unexpired term of one year or less to maturity, (or to the earliest call date where a transaction is completed at a premium).
- 3) All Government of Canada Bonds and Government of Canada Guaranteed Bonds having an unexpired term of over one year but three years or less to maturity (or to the earliest call date where a transaction is completed at a premium) shall be traded in multiples of five cents.
- 5) (a) Unless prefixed by some qualifying phrase, a dealer calling a market shall be obliged to trade Trading Units (as hereinafter defined), if called upon to trade;
(b) Any dealer asking the size of a stated market must be prepared to buy or sell at least a Trading Unit (as hereinafter defined) at the price quoted if immediately requested to do so by the member calling the market;
(c) Trading Units shall consist of the following:
 - (i) In the case of Government of Canada direct obligations and Government of Canada



EXHIBIT "E"

TRADING RESTRICTIONS - JANUARY 1, 1951

All transactions by dealers, whether acting in the capacity of either principal or agent, shall be as follows:-

- 2) There are no spread restrictions regarding trading of Government of Canada Bonds and Government of Canada Guaranteed Bonds having an unexpired term of one year or less to maturity, (or to the earliest call date where a transaction is completed at a premium).
- 3) All Government of Canada Bonds and Government of Canada Guaranteed Bonds having an unexpired term of over one year but three years or less to maturity (or to the earliest call date where a transaction is completed at a premium) shall be traded in multiples of five cents.
- 5) (a) Unless prefixed by some qualifying phrase, a dealer calling a market shall be obliged to trade Trading Units (as hereinafter defined), if called upon to trade;
- (b) Any dealer asking the size of a stated market must be prepared to buy or sell at least a Trading Unit (as hereinafter defined) at the price quoted if immediately requested to do so by the member calling the market;
- (c) Trading Units shall consist of the following:
 - (1) In the case of Government of Canada direct obligations and Government of Canada



1 Guaranteed obligations having an
2 unexpired term of three years or less
3 to maturity (or to the earliest call date,
4 where the transaction is completed at a
5 premium); \$100,000 -- par value.

6 (ii) In the case of Government of Canada
7 direct obligations and Government of Canada
8 Guaranteed obligations, having an unexpired
9 term to maturity of longer than three years
10 (where a bond is traded at a premium the
11 earliest call date shall be treated as the
12 maturity date); \$25,000 -- par value.

13 (iii) In the case of all other bonds and
14 debentures other than Government of Canada
15 direct obligations and Government of
16 Canada Guaranteed obligations; \$5,000
17 -- par value.

18 (iv) In the case of bonds and debentures
19 issued with attached stock, warrants rights,
20 or other appendages and traded in unit form;
21 \$5,000 par value of Bonds or Debentures,
22 irrespective of the value of the appendages.

23 (v) In the case of common and preferred
24 shares not listed on a recognized stock
25 exchange (as defined in the Regulations of
26 the I.D.A.)

- 27 -- in lots of 500 shares, if market price is below \$1
28 -- in lots of 100 shares, if market price is at \$1 and
29 below \$100
30 -- in lots of 50 shares, if market price is at \$100
 or above.



Unredeemed Debentures Having an

unexpired term of three years or less
to maturity (or to the earliest call date,
where the transaction is completed at a

premium) (iii) -- par value.

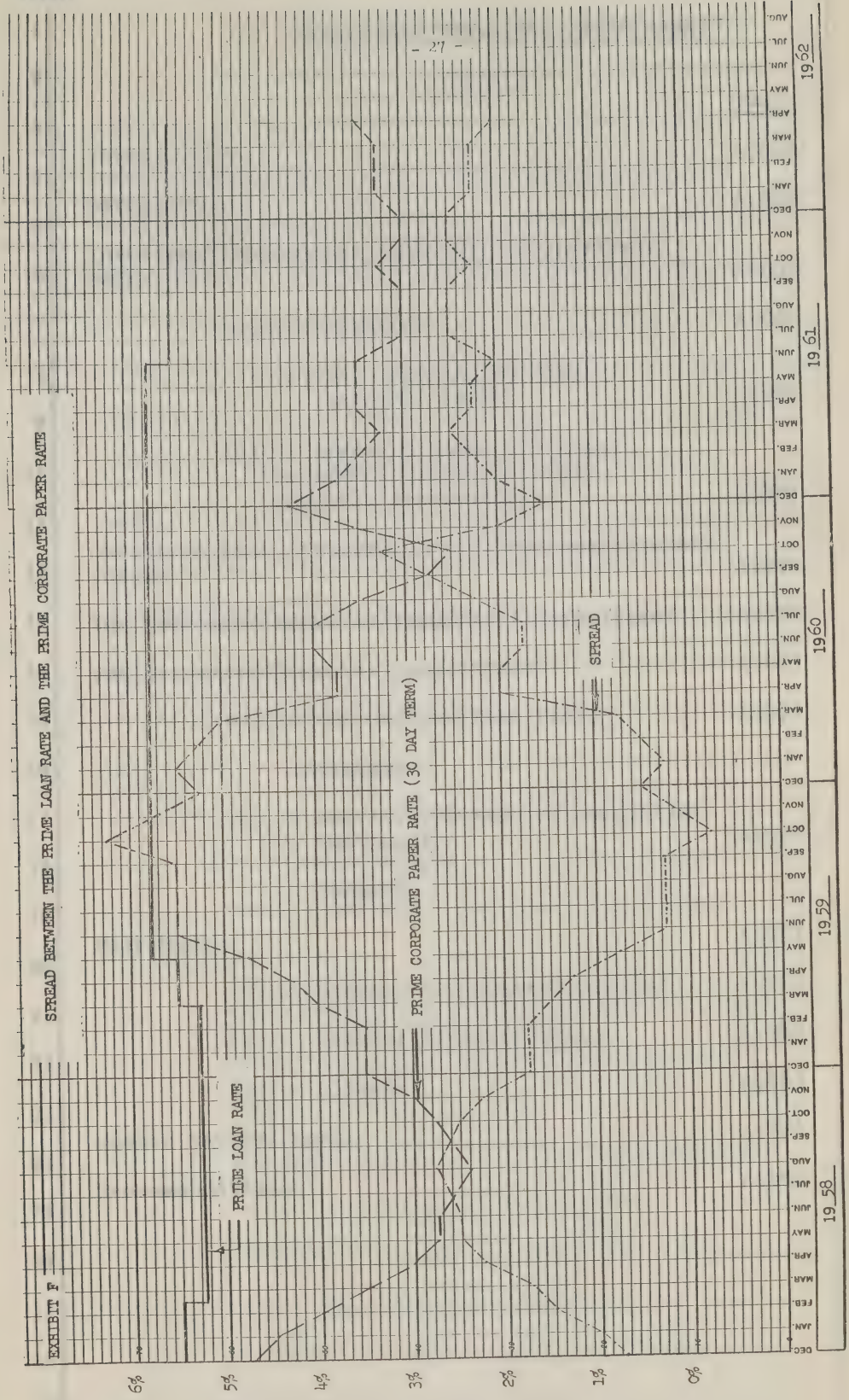
(ii) In the case of Government of Canada
direct obligations and Government of Canada
guaranteed obligations, having an unexpired
term to maturity of longer than three years
(where a bond is traded at a premium the
earliest call date shall be treated as the
maturity date); \$25,000 -- par value.

(iii) In the case of all other bonds and
debentures other than Government of Canada
direct obligations and Government of
Canada guaranteed obligations; \$5,000
-- par value.

(iv) In the case of bonds and debentures
issued with attached stock, warrants rights,
or other appendages and traded in unit form;
\$5,000 par value of Bonds or Debentures,
irrespective of the value of the appendages.

(v) In the case of common and preferred
shares not listed on a recognized stock
exchange (as defined in the Regulations of
the I.D.A.)

-- in lots of 500 shares, if market price is below \$1
-- in lots of 100 shares, if market price is at \$1 and
below \$100
-- in lots of 50 shares, if market price is at \$100
or higher.



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1900



CHARTERED BANKS and "NEAR BANKS"

I N D E X

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CHARTERED BANKS and "NEAR BANKS"

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1 CHARTERED BANKS and "NEAR BANKS"

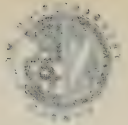
2 1. There is a close relationship between the
3 business of the investment Dealer and the Canadian
4 banking community. Accordingly, it is of prime
5 importance that the Investment Dealer keep abreast of,
6 and closely in tune with, changes that occur in banking
7 policies and practices that may in any way affect the
8 market for, and best possible distribution of, investment
9 securities. It is appropriate that full advantage
10 be taken of the investigations being made by this
11 Commission to outline the existing relationships between
12 the investment Dealer industry and the Chartered Banks
13 and "Near-Banks", and to closely examine these relation-
14 ships in a search for ways of improving the functioning
15 of the whole capital market.

16 2. DEFINITIONS -- For the purposes of this
17 presentation, we shall define --

18 (a) Chartered Banks -- as those Banks
19 which come under the provisions of the
20 Bank Act.

21 (b) Quebec Savings Banks -- as those Banks
22 which come under the provisions of the
23 Quebec Savings Bank Act.

24 (c) Near-Banks -- All other institutions
25 which receive deposits (some times with
26 chequing privileges) and/or make loans,
27 e.g., Trust Companies, Mortgage and Loan
28 Companies, Caisses Populaires, Credit
29 Unions and, in some aspects of their
30 operations, Finance Companies, Small



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1 Loan Companies, Provincial and Municipal
2 Governments and Industrial and Commercial
3 Corporations.

4 INVESTMENT DEALERS AS CUSTOMERS OF CHARTERED BANKS

5 (a) As borrowers

6 3. The nature of our business, involving
7 periodic underwritings, and the carrying from day-to-day
8 of large inventories of securities, requires large scale
9 borrowing by way of, what are known as, call loans and
10 day loans. These loans are secured by the deposit of
11 securities pending sale or delivery. It is important
12 that such loans be readily available at minimum cost.

13 4. The Chartered Banks at one time were
14 virtually the only source of such funds. In recent
15 years other sources have appeared and assumed growing
16 significance.

17 5. Call loans and day loans to Investment
18 Dealers carry a high credit rating involving a minimum
19 risk. As evidence of their quality, the Bank of Canada
20 includes these loans in their banking statistics under
21 the heading "More Liquid Assets", along with Bank of
22 Canada Notes and deposits, Treasury Bills, Government
23 Bonds and net Foreign Assets. They are highly acceptable
24 means of employing cash not immediately needed elsewhere.

25 6. The demand for these loans is constant
26 in nature, although fluctuating some times widely, in
27 amount. (See Exhibits A.1, A.2, A.3).

28 7. The revenue accruing to the Chartered
29 Banks as well as to other lenders arising from interest
30 charges on these loans is shown in Exhibit B.



Loan Companies, Provincial and Municipal
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INVESTMENT BANKING AS A SOURCE OF CREDIT

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Banks as well as to other lenders arising from interest
charges on these loans is shown in Exhibit B.



8. A special scale of interest rates usually graduated upwards by several categories of collateral from the shortest term most liquid, to the longer term less liquid, is applied by the banks to such loans. These graduations are inferred to be related to market yield rates for such collateral, with appropriate changes made as circumstances warrant.

9. In practice, however, the dealers have found an element of rigidity built into these scales, particularly during periods of heavy demands for commercial loans (e.g., schedule unchanged from August 10, 1959 to October 11, 1960, remaining at flat 5 3/4 per cent rate for all categories, except two, of collateral, although bond yields, as shown below, fell sharply during that period, e.g.,

Canada 3 3/4%	Sept.1/65	Aug.26,1959	88 1/4	6.12%
		Sept.28,1960	98 1/2	4.07
4 1/2%	1983	Aug. 26,1959	87 3/8	5.45
		Sept.28,1960	94 11/16	4.89

During this same 14 months' period, the re-discount rate declined from 6.41 per cent on Aug. 13, 1959 to 1.95 per cent on September 29, 1960.

10. Also the date, when these high rates were applied, virtually coincided with the date when bank general loans, having increased by 24 per cent or \$1,211 million between Oct. 1, 1958 and Aug. 19, 1959 levelled off and then declined between August 19th and Dec. 31st, by \$213 million. This downward trend continued during the first quarter and then turned upward again somewhat more than seasonally for the



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1 remainder of 1960. Throughout this period call loan
2 rates remained unchanged.

3 11. It is recognized that Sec. 91 of the Bank
4 Act and Sec. 71 (1) of the Quebec Savings Bank Act,
5 placing a ceiling of 6 per cent on the rate of interest
6 banks may charge, inhibits the banks, in periods of
7 excessive demand for loans, from using "price" as a
8 restraint on general loan expansion, induces a type of
9 loan rationing, and contributes to lack of flexibility
10 when interest rates start to decline.

11 12. It must also be recognized, however,
12 that this "price" factor, especially during the 14 months
13 referred to above, did contribute directly to the
14 development of a large and significant alternate source
15 of short term funds for the Investment Dealer -- the so-
16 called "Country Banks", an expression particular to our
17 industry but for the purpose of this Brief included in
18 the definition of "Near-Banks". The dealers, in the
19 face of apparent indifference on the part of the
20 Chartered Banks, sought out other sources of accommodation
21 with no little success.

22 13. If the dealer could be satisfied that the
23 call loan interest rates of the banks were subject to
24 periodic review and appropriate action to keep them in
25 line with market conditions, and competitive with non-
26 bank rates, many of the call loans being obtained in
27 the Country Banking System, in all probability, would
28 revert to the Chartered Banks. Costs being reasonably
29 close, the dealer, generally speaking, would prefer to
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1 The Ceiling on Bank Interest Rates -- The Bank Act -
2 Section 91.

3 14. "Except as provided in subsection (2),
4 no bank shall in respect of any loan or advance payable
5 in Canada stipulate for, charge, take, reserve or exact
6 any rate of interest or any rate of discount exceeding
7 six per cent per annum and no higher rate of interest
8 or rate of discount is recoverable by the bank." A
9 similar restriction appears in Sec. 71 (1) of the
10 Quebec Savings Bank Act.

11 15. We believe that this provision, in periods
12 of financial stringency, prevents the banks from using
13 "price" as a deterrent to undesirable loan expansion.
14 When loaning resources become strained, the Banks must
15 resort to a form of rationing, with the attendant dangers
16 of discrimination as between different classes of
17 borrowers.

18 16. The Near-Banks, to whom the ceiling does
19 not apply, can use higher interest earnings to pay higher
20 rates on deposits and so gain an advantage over the
21 Chartered Banks.

22 17. Our Association believes that this
23 interest ceiling should be removed, as was recommended
24 in the McMillan Report 1933. Chapter VII para. 253 --
25 "Four of us are of opinion that a statutory maximum rate
26 of interest is nowadays anomalous and an undesirable
27 interference with freedom of contract....by a majority,
28 we recommend the repeal of the provision in question."
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Investment Dealers as Customers of Chartered Banks (cont'd)

(b) As users of bank facilities to effect deliveries and complete transactions.

18. The Chartered Banking System provides the dealer with invaluable service facilities contributing materially to the quick, convenient completion of transactions and deliveries of securities.

19. There is, however, an area within this field, involving daylight overdrafts, where unacceptably high bank charges have led the dealer to devise a rather cumbersome but effective means of reducing the impact of these costs.

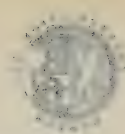
20. It is suggested that a joint committee of the I.D.A. and the C.B.A. might be constituted to which these and other problems of mutual concern could be referred for frank discussion and possible solution.

THE BANKS AS AN IMPORTANT SECTOR IN THE MARKET FOR SECURITIES

21. As a custodian of the bulk of the personal savings deposits of millions of Canadians, the manner in which these assets are employed is of major significance to the economy as a whole and certainly to the security markets.

22. At the end of 1945, savings deposits stood at \$2,865 million. At the same time, Government of Canada and Provincial securities owned by the banks amounted to \$3,586 million, of which \$1,415 million were under two years in term.

23. By the end of 1946, personal savings had grown to \$3,476 million, with the holdings of Canada and Provincial bonds rising to \$3,693 million, of which



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1 \$1,308 million were under two years in term.

2 24. This state of affairs led to an agreement
3 effective March 1, 1946 on the part of the chartered
4 banks with the Bank of Canada that their investments in
5 Government of Canada, direct and guaranteed issues
6 (other than Treasury Bills, Deposit Certificates and
7 Treasury Notes), would not average more than 90 per cent
8 of the amount of their Canadian personal savings deposits.
9 The banks also agreed that their earnings on such bonds
10 should not exceed the cost of operating their savings
11 business by more than a moderate profit margin. (Bank of
12 Canada Report 1946 - page 14....Since cancelled as no
13 longer necessary or desirable.)

14 25. In the following year, there was a net
15 decline of \$170 million in Chartered Bank holdings of
16 Government of Canada bonds, but their holdings of
17 Provincial and Municipal securities increased by \$159
18 million and their portfolio of other non-Government
19 securities -- largely corporate debentures -- by \$147
20 million. In that year, the Chartered Banks accounted
21 for \$316 million of a total of \$327 million net increase
22 in Canadian bonds and stocks outstanding.

23 26. The extent of the Chartered Banks'
24 participation in the market for non-Government securities
25 diminished in importance from this point onward, with
26 other investors absorbing almost all the large net
27 increase of non-Government securities. (See Statistical
28 Table - Bank of Canada - Exhibit C).

29 27. Since 1948, the Chartered Banks have
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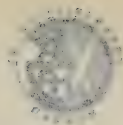
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1 commercial loans. It is only when the demand for short-
2 term loans lessens that the banking system becomes a
3 purchaser of securities. As a corollary, an increase
4 in the demand for loans leads to the selling of
5 securities by the banking system. The investment
6 function is residual to the loaning function.

7 28. The attached statistics (Exhibit D) show
8 the security holdings by category of the chartered banks
9 for the past sixteen years. As can be readily seen, the
10 holdings of Government of Canada securities (including
11 treasury bills) is by far the most volatile type of
12 investment. In respect to holdings of Government of
13 Canada securities beyond the two year area, it may be
14 assumed that the vast majority mature within a five year
15 period. In addition, maturity holdings beyond a ten
16 year period are likely to be an exception. Generally,
17 provincial holdings are well within the ten year
18 maturity range. As to municipals, bank purchases fall
19 within the 1 - 10 year range, the choice depending upon
20 money position and interest in the municipality
21 involved. The holdings of corporate securities are
22 normally limited to under the ten year area, with, however,
23 some exceptions being made for special bank clients.
24 The acquisition of term corporation securities, wherein
25 a chartered bank purchases all or a large portion of a
26 private placement has, since 1955, been subject to
27 restrictions arising out of an agreement amongst the
28 Chartered Banks which has been varied from time to time
29 in light of conditions. We concur in the desirability
30 of these restrictions.



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1 CHARTERED BANK INVESTMENT PRACTICES AND MONETARY POLICY

2 29. The residual nature of Chartered Bank
3 investment policy subjects the market place to rather
4 violent swings in security prices and yields. The
5 effect is particularly evident in short-term Government
6 of Canada securities. An example of this effect, and the
7 resultant effects on the whole interest rate structure,
8 was evident in 1959 when the banking system, with demand
9 for short term loans inordinately high, was a substantial
10 seller of short term securities, thereby driving the
11 yield of two year Canada through 6 per cent. During the
12 following two years, the banking system was a net
13 purchaser of short term securities and the yield on two
14 year Canadas declined to as low as $3\frac{1}{2}$ per cent.

15 30. Referring to pages 27 - 31 of the Bank of
16 Canada Report of 1956 (Exhibit E) the Governor describes
17 a serious weakness in the monetary control mechanism.
18 The events of 1959 demonstrate the ineffectual use of
19 monetary controls when the banking system has the liquidity
20 to thwart the desired results of the control measures.
21 The attached statistics (Exhibit D) indicate that during
22 the past eleven years, the Chartered Banks have placed
23 an increasing percentage of their assets in Government of
24 Canada securities maturing under two years. During the
25 same period, a decreasing percentage of those assets
26 have been invested in all securities maturing over two
27 years. When considered in relation to personal savings
28 deposits, the decline in the ratio of security holdings
29 maturing over two years to personal savings deposits is
30 evident. (Exhibit F).



MONETARY BANKING AND FINANCIAL SYSTEMS

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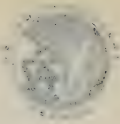
evident. (Exhibit F).



1 31. It is clear that the liquidity position
2 of the banking system has been enhanced considerably
3 during this period to the point where the desires of the
4 monetary authorities might be effectively thwarted.

5 32. If it is considered desirable to attempt
6 to reduce the long term interest rate on Canadian
7 securities in order to moderate the flow of long term
8 foreign investment, and, at the same time, establish the
9 foreign exchange values of the Canadian dollar commensurate
10 with the balance of trade position of the nation, the
11 savings of the Canadian people would have to be mobilized
12 to a maximum degree, and a proper proportion shepherded
13 into the kind of investment naturally associated with
14 long term savings. This suggests as an avenue of
15 exploration the possibility that personal savings deposits
16 held by the Chartered Banks, which have shown a steady
17 upward trend (Exhibit F), might be made available to a
18 greater extent than at present is the case for long term
19 investment.

20 33. This whole question is discussed at
21 considerable length in the Bank of Canada Annual Report
22 1956. (Exhibit E). The suggestions developed therein
23 might well be examined in the light of present day
24 conditions. In the words of that report: "The
25 possibility of a gradual approach towards arrangements
26 of the sort outlined would seem to be worthy of study
27 and discussion. Progress in such an approach would be
28 directed towards expanding mortgage loans and other
29 appropriate investments based on future increases in
30 savings deposits, not reducing the volume of commercial



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1 or general loans."

2 THE CHARTERED BANKS AS ISSUERS OF SECURITIES

3 34. Though the chartered banks have offered
4 term deposit receipts to their clients for a good number
5 of years, it has been only during the past two years
6 that the instrument has been an effective competitive
7 vehicle in the market place. In severe competition for
8 the funds of the large depositor (\$100,000 plus) with
9 the "near-banks", the chartered banks offer term deposit
10 receipts at various rates for terms up to one year. The
11 volume of such deposits is unknown but considered to be
12 substantial. A number of chartered banks also offer
13 term deposit receipts for terms of one to five years at
14 competitive rates. On this type of paper, the chartered
15 bank may pay a commission to the investment dealer which
16 secures the funds on its behalf. Again, volume figures
17 are not published. Another vehicle of investment that the
18 banking system offers from time to time to the potentially
19 larger short-term depositor is what is usually called a
20 U.S. Dollar Term Deposit. The chartered bank accepts
21 the deposit at a given rate for a specific term, swaps
22 the funds into U.S. dollars, with the profit or loss on
23 the swap payable to the depositor, and invests the U.S.
24 funds in the New York call loan market. This instrument
25 has, at times, proven to be highly competitive vehicle,
26 wherein rates obtainable can be appreciably better than
27 what is available in the domestic market for similar
28 quality.

29 35. In respect to term deposit receipts
30 maturing within one year, rates are established by



THE CHARTERED BANKS AS ISSUERS OF SECURITIES

term deposit receipts to their clients for a good number of years, it has been only during the past two years that the instrument has been an effective competitive vehicle in the market place. In severe competition for the funds of the large depositor (\$100,000 plus) with the "near-banks", the chartered banks offer term deposit receipts at various rates for terms up to one year. The volume of such deposits is unknown but considered to be substantial. A number of chartered banks also offer term deposit receipts for terms of one to five years at competitive rates. On this type of paper, the chartered bank may pay a commission to the investment dealer which secures the funds on its behalf. Again, volume figures are not published. Another vehicle of investment that the banking system offers from time to time to the potential larger short-term depositor is what is usually called a U.S. Dollar Term Deposit. The chartered bank accepts the deposit at a given rate for a specific term, swaps the funds into U.S. dollars, with the profit or loss on the swap payable to the depositor, and invests the U.S. funds in the New York call loan market. This instrument has, at times, proven to be highly competitive vehicle, wherein rates obtainable can be appreciably better than what is available in the domestic market for similar

35. In respect to term deposit receipts

maturing within one year, rates are established by



1 agreement between banks. On a number of occasions in
2 the past two years, it has been demonstrated that the rate
3 changes have not responded quickly to market conditions.
4 It is probable that this lack of responsiveness is being,
5 and will be, corrected in the future. In the case of
6 term deposits maturing over one year, rates are determined
7 independently, governed by returns obtainable in the
8 employment of these deposits.

9 THE BANKS AND NEAR-BANKS AS COMPETITORS

10 36. The Investment Dealer must regard as a
11 competitor any person or agency that performs, or offers
12 to perform, any of what the dealer regards as his
13 functions. Outlined below are some of the ways, and
14 extent to which, the Banks and Near-Banks appear to
15 invade our field.

16 (a) In the Underwriting Field

17 Canada and Canada Guaranteed Issues

18 37. Just as the dealers are offered varying
19 percentages of each issue on a "firm" basis, so are the
20 chartered banks, usually at the same concession from the
21 sale price to the public. Since these are drawn down
22 for resale, they are underwritings. Bonds purchased
23 for the banks' own portfolio requirements, at the time
24 of issue, are of course taken at the full issue price.

25 Provincial and Provincial Guaranteed Issues

26 38. One or more chartered banks are included
27 in each syndicate formed to bid for, or negotiate the
28 purchase of, provincial or provincial guaranteed bonds.
29 They take an active part in the discussions, and are
30 influential in the decisions reached, regarding terms.



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1 The judgment of the bank which carries the banking
2 account of the province concerned may carry especial
3 weight, both as an adviser to the Province and within
4 the syndicate. They participate in syndicate profits
5 according to their established interest in the account,
6 which interest is not necessarily supported by
7 demonstrated placing power.

8 Municipals and Municipal Guaranteed Issues

9 39. As with provincial issues, one or more
10 chartered banks are frequently included in the syndicate's
11 bidding for, or negotiating the purchase of, municipal
12 debenture issues, particularly in the case of large
13 municipalities. Where serial issues are involved, and
14 these are in the majority, the banking member or
15 members of the syndicate not infrequently agree to
16 purchase for their own account the early maturities.
17 So the degree of enthusiasm shown by the banking members
18 has a direct bearing on the price finally agreed upon.

19 40. Again, the banking members share,
20 according to their interest, in any syndicate profits
21 that emerge -- and again their interest in the syndicate
22 does not necessarily bear a relationship to their
23 contribution as a distributor.

24 Corporate Issues

25 41. The involvement of banks in underwriting
26 of corporate issues is much less usual than in the case
27 of government financing. The Bank Act (Para. 157(2))
28 forbids the use of the name of any chartered bank "in
29 a prospectus of advertisement for the sale of securities
30 of any kind other than those issued by, or guaranteed



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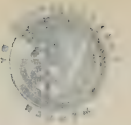
1 as to principal and interest by, Canada". The Chartered
2 Banks agreed in 1955 to "cease making new commitments for
3 term lending, that is, making loans (in excess of
4 \$250,000) (Subsequently raised to \$1,000,000) to business
5 corporations where the time of repayment is deferred
6 beyond that of ordinary bank loans, or purchasing a
7 security negotiated directly with the customer as distinct
8 from buying a publicly issued security in the market."
9 (Bank of Canada Report 1956).

10 42. This Section of the Bank Act, and the
11 agreement referred to, which agreement we understand
12 has been renewed and somewhat expanded from time to time,
13 clearly implies intended definite limitations as to the
14 extent to which the chartered banks should venture into
15 the field of distribution of securities other than those
16 issued by governments, and into the corporate underwriting
17 field.

18 43. Nonetheless, there are important instances
19 where chartered banks are members of, and actively
20 participate in the management of, syndicates formed for
21 the purpose of underwriting securities of large
22 corporations.

23 Comments on Banks as Members of Underwriting Syndicates

24 44. The question as to whether the public
25 interest or any useful purpose is served through the
26 inclusion of chartered banks in underwriting syndicates
27 is one upon which there is considerable disagreement
28 amongst our members. It is recognized that many of
29 these arrangements were entered into many years ago,
30 probably when there were good reasons for them. The Brief



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submitted by this Association to the Royal Commission on Banking and Currency in Canada in 1933 points out that immediately after the First War the capital requirements of governments, municipalities and industrial corporations were very large. Special arrangements were necessary to deal with them. The Brief stated: "Due to the size and number of issues offered, syndicates would include one or more banks as syndicate members, giving the bank (in addition to interest on the loan required) a share in the syndicate profits for its agreement to finance the issue pending distribution. It should be noted here that the bank's share of the profits was purely remuneration for carrying the loan and for its proportionate liability in the account, and the bank was not expected to, and in the early years did not, itself distribute bonds."

45. The investment banking industry of those days was in the early stages of its development. It possessed only a small measure of the experience and financial strength that it has since acquired. Over the intervening years, the industry has matured and has demonstrated its ability to cope with the challenges with which it has been faced in meeting the capital needs of the Government of Canada, of other governments and public bodies, and of credit-worthy corporations. No longer is it necessary to hold out the golden carrot of a share of syndicate profits to obtain the banking accommodation it requires to fulfil its commitments. The fact remains that one or more chartered banks are members of most municipal syndicates of any size, of all



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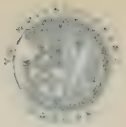
1 of the provincial syndicates, and of a few of the
2 important corporation syndicates.

3 46. Those of our members who take no exception
4 to these arrangements maintain that the presence of
5 banks in municipal syndicates adds strength to the bids
6 where their banking partner agrees to absorb the early
7 maturities. In provincial syndicates where the issues
8 are set up on a fiscal agency basis, they acknowledge
9 that the presence in the syndicates of the Province's
10 bankers is helpful in negotiations. When negotiations
11 are completed and liabilities taken, the assumption by
12 the banking syndicate members of their share of the
13 risks involved is reassuring to many of the syndicate
14 members. During the process of distribution, the
15 manner in which the banks deal with their participations
16 may aid orderly distribution and lend stability to the
17 after market.

18 47. In those relatively few cases of
19 membership in corporate syndicates where the relation-
20 ships are of relatively long standing, many of our
21 members would not press to have these relationships
22 disturbed. The majority of our members, however,
23 would strongly discourage any extension of the practice.

24 48. Those of our members who object to the
25 presence of chartered banks in underwriting syndicates
26 support their position with these arguments:

27 (a) There are many possibilities of
28 undesirable conflicts of interest arising
29 out of intermingled customer relationships,
30 particularly where the bank assumes the



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would strongly discourage any extension of the practice.

49. Those of our members who object to the

presence of chartered banks in underwriting syndicates

submit the following reasons:

(a) There are many possibilities of

undesirable conflicts of interest arising

out of intermingled customer relationships,

particularly where the bank assumes the



1 role of syndicate management.

2 (b) The primary function of the chartered
3 banks is to provide for the short-term
4 capital needs of its customers, whether
5 public or private. The primary function
6 of the Investment Dealer is to find long-
7 term capital for both governments and
8 corporations.

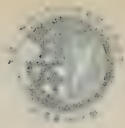
9 (c) It is in the public interest and
10 important to the Chartered Banks them-
11 selves that the investment banking
12 industry maintain a healthy growth
13 consonant with the growth of the
14 country's economy. The curtailment of
15 the dealer's field of activity through
16 undue invasion and penetration by the
17 Chartered Banks is bound to inhibit the
18 growth and development of the investment
19 dealer industry and so its ability to
20 adequately perform its proper function
21 within the economy.

22 49. The common ground within the conflicting
23 points of view of our members is that there be no
24 extension of the practice of including chartered banks
25 within underwriting syndicates nor delegation to them
26 of the management function.

27 The Banks and Near-Banks as Competitors

28 (b) In Distribution of Securities to the Public

29 50. The Chartered Banks, and to a lesser but
30 significant extent the Near-Banks, actively engage in the



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The Banks and Non-Banks as Competitors

(d) In Distribution of Securities to the Public
50. The Chartered Banks, and to a lesser but significant extent the Non-Banks, actively engage in the



1 sale of securities to the public as agents and, not
2 infrequently, as principals. They enjoy peculiar
3 advantages over the dealers through their widespread
4 branch systems, with only incidental distribution costs,
5 and possessing knowledge of their customers' resources.

6 (1) As officially named and recognized agents

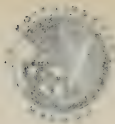
7 and receiving the same selling commissions
8 as the Dealers, the Chartered Banks and the
9 Trust Companies participate in the distribution
10 of Canada Savings Bond issues and in the newly
11 emerged type of provincial parity bonds. It
12 is worth noting that this type of distribution
13 does not involve positions or risk, nor the
14 exercise of investment judgment. In addition
15 to selling commissions, the banks receive
16 remuneration as issuing agents, thereby
17 profiting from the successful efforts of the
18 Dealers.

19 (2) As members of Selling Groups -- In those

20 new issues where Selling Groups are formed,
21 the usual procedure is to include all members
22 of the I.D.A. and the Chartered Banks. This
23 entitles the Banks to acquire the securities
24 involved on the same basis as do the Dealers.

25 (3) As principals -- in issues where the

26 Banks are members of underwriting syndicates.
27 Here it is assumed that the Banks utilize
28 their securities departments in the
29 distribution of their participation. The
30 Banks also, in a substantial way, act as



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principals in their secondary market

operations.

Comments on Banks as distribution of securities to the public

51. It is recognized that the Canadian Chartered Banks with their comprehensive branch system, and intermingling in their operations as they do commercial and savings bank functions -- functions which elsewhere are usually separated -- have an advantage over the Dealer in reaching the potential investor at low and only incidental cost. Their effectiveness in Canada Savings Bond and similar campaigns is acknowledged, as is also their usefulness in serving the investment requirements of the customers of branches in small communities beyond the reach of investment houses. The Dealers, to offset these advantages, rely upon their specialized training and knowledge and concentration upon their particular functions.

52. In view of the reliance placed by the Chartered Banks on savings deposits as a funds source from which to expand commercial loans, there arises the question of conflict of interest, the conceivable tendency on the part of individual branch managers to discourage investment in order to maintain savings deposits. This could happen at the very time non-bank buyers are needed to absorb the pressure on the bond market of sales of securities by the banks to meet heavy demand for loans. At such times the burden of finding buyers falls on the investment dealer sales force and it is important that such sales force be available, in



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sufficient size, vigorous and resourceful enough, to do an effective job.

"NEAR-BANKS"

53. In our definitions, "near-banks" were described as institutions which perform one or more banking function, i.e. -- receive deposits and/or loan funds. As examples, we mentioned trust companies, caisses populaires, credit unions, finance companies, small loan companies, mortgage companies, corporations and provincial and municipal governments. Though it can be said that every financial intermediary performs one or more banking functions, the growth and the competitiveness evidenced in the above-mentioned institutions have made them subject to an increasing amount of comment in recent years.

54. We wish to discuss the relationship of these financial institutions to the investment dealer and to comment upon the impact on the financial framework of the nation consequent upon the growth in their resources.

RELATIONSHIP OF "NEAR-BANKS" TO INVESTMENT DEALER

(a) As Sources of Borrowed Capital

55. As a result of the inadequacy and cost of chartered bank accommodation during various periods in the last ten years, the trust company, the provincial and municipal government and the corporate entity have become important suppliers of demand and term funds to the investment industry. The volume of such loans is indicated in the weekly figures that have been collected by this Association since November of 1960. Were it not



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WEAR-BANKS

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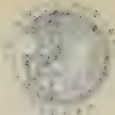
1 for the availability of these funds there is little doubt
2 the investment dealer costs would have been greater during
3 the past three years.

4 56. As well as providing funds to investment
5 dealers, the "near-bank" also provides short term funds
6 to other financial intermediaries, e.g. -- corporate
7 borrowers, finance companies and provincial and municipal
8 governments. Although the volume of such loans out-
9 standing at any one time is intermediate, there is reason
10 to believe that it would be very considerable.

11 (b) As Issuers of Securities

12 57. The "near-bank" offers a considerable
13 variety of securities ranging from demand deposits to
14 debentures, to deposit receipts, to certificates of
15 deposits, to short term promissory notes and to secured
16 or unsecured finance paper. Terms can vary from one day
17 to five years and in size from \$1,000 to millions of
18 dollars. The securities are offered directly to the
19 general public by some of these institutions, while
20 others deal only through investment dealers, who act as
21 principals or agents in the placement of these securities.
22 Most of the "near-banks" attempt to secure their funds
23 by both avenues. The investment dealer, when acting as
24 an agent, obtains a commission for his service. When
25 performing as a principal, the dealer re-offers the
26 security at a price that will provide a profit.

27 58. There has been concern expressed in
28 recent years as to the responsibility of the dealer in
29 the placement of the securities of "near-banks". The
30 pressure exerted within a firm to secure funds for a



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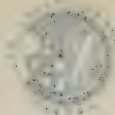
1 client have, undoubtedly, resulted in the placement of
2 securities of dubious quality. We believe that the
3 investment dealer must bear responsibility for the quality
4 when the investing client is not in a position to judge
5 the credit risk. The sophisticated investor requires
6 no such protection. It is the belief of this
7 Association that any rules and regulations in this
8 respect could be easily circumvented.

9 (c) The "Near-Banks" as Clients

10 59. The growth in assets of some of the
11 institutions included in the category "near-banks" is
12 graphically represented in the attached exhibits. We
13 have shown the substantial increase in bonds, mortgage
14 and stock holdings of the trust and loan corporations
15 and in the investments (No published breakdown of these
16 investments is available covering all credit unions but
17 the Province of Quebec report on Caisses Populaires for
18 1960 indicates that over 75 per cent of the total
19 investments of all credit unions were held by the
20 "Caisses" of that Province, distributed as follows:

21 Canadian Government Bonds	\$ 24,092,466
22 Provincial Government Bonds	34,905,525
23 Municipal or School Corporation Bonds	105,800,943
24 Church Fabric Bonds, Ecclesiastic and Religious Corporation Bonds	47,226,664
25 Total	\$212,025,598)

26
27 of credit unions during the past ten years. The
28 attached statistics for Canadian trust companies also
29 demonstrate the substantial growth that has taken place
30 in the past ten years in assets under administration,



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(c) The "Near-Banks" as Classes

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1 i.e. -- estates, trusts and agency funds. When it is
2 considered that these statistics cover the assets of
3 only certain of the "near-banks", it is evident that these
4 institutions have a significant impact on the market-
5 place.

6 QUEBEC SAVINGS BANKS

7 The attached statistics (Exhibit 1) show the
8 extent to which the assets of the Quebec Savings Banks
9 are invested in Canadian securities.

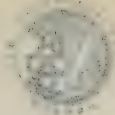
11 RECOMMENDATIONS

12 It is recommended to the Commission that
13 consideration be given to the following suggestions:

14 (1) that the chartered banks adopt policies
15 and procedures designed to satisfy the invest-
16 ment dealers that their call loan interest
17 rate schedules are to be subject to periodic
18 review and appropriate action to keep them
19 in line with market conditions and competitive
20 with the rates under which similar loans may
21 be obtained from non-bank sources.

22 (2) that Section 91 of the Bank Act and
23 Section 71 (1) of the Quebec Savings Bank Act,
24 imposing a ceiling of 6 per cent on the rate
25 which may be charged upon bank loans, be
26 repealed as being "an undesirable interference
27 with freedom of contract."

28 (3) that every encouragement should be given
29 to the continued healthy development of the
30 Investment Dealer's ability to perform



1.e. -- estates, trusts and agency funds. When it is considered that these statistics cover the assets of only certain of the "near-banks", it is evident that these institutions have a significant impact on the market place.

CONCLUSIONS

The attached statistics (Exhibit 1) show the extent to which the assets of the Quebec Savings Banks are invested in Canadian securities.

RECOMMENDATIONS

It is recommended to the Commission that consideration be given to the following suggestions:

(1) that the chartered banks adopt policies and procedures designed to satisfy the investment and business needs of their customers.

rate schedules are to be subject to periodic review and appropriate action to keep them in line with market conditions and competitive with the rates under which similar loans may be obtained from non-bank sources.

(2) that Section 91 of the Bank Act and Section 71 (1) of the Quebec Savings Bank Act, imposing a ceiling of 6 per cent on the rate which may be charged upon bank loans, be repealed as being "an undesirable interference with freedom of contract."

(3) that every encouragement should be given to the continued healthy development of the investment dealer's ability to perform

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satisfactorily the important underwriting
function and in particular:

(a) that the banks continue to refrain
from making term loans (in excess
of a reasonable limit in amount)
to business corporations where the
time of repayment is deferred beyond
that of ordinary bank loans, or
purchasing a security negotiated
directly with the customer as
distinct from buying a publicly issued
security in the market.

(b) that there should be no further
extension, beyond the relatively few
cases of long standing which may
exist, of the inclusion of banks in
syndicates underwriting corporate
securities for resale to the public,
particularly where such inclusion
would place the bank in the dual
position of banker and underwriter
and where the sale of corporate
securities is for the purpose of
paying off bank loans.

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ALTERNATIVE TO THE EXISTING SYSTEM
OF BANKING AND CREDIT

(a) that the banks continue to refrain from making term loans (in excess of a reasonable limit in amount) to business corporations where the time of repayment is deferred beyond that of ordinary bank loans, or purchasing a security negotiated directly with the customer as distinct from buying a publicly issued security in the market.

(b) that there should be no further extension, beyond the relatively few cases of long standing which may exist, of the inclusion of banks in syndicates underwriting corporate securities for resale to the public, particularly where such inclusion would place the bank in the dual position of banker and underwriter and where the sale of corporate securities is for the purpose of paying off bank loans.

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and
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EXHIBITS

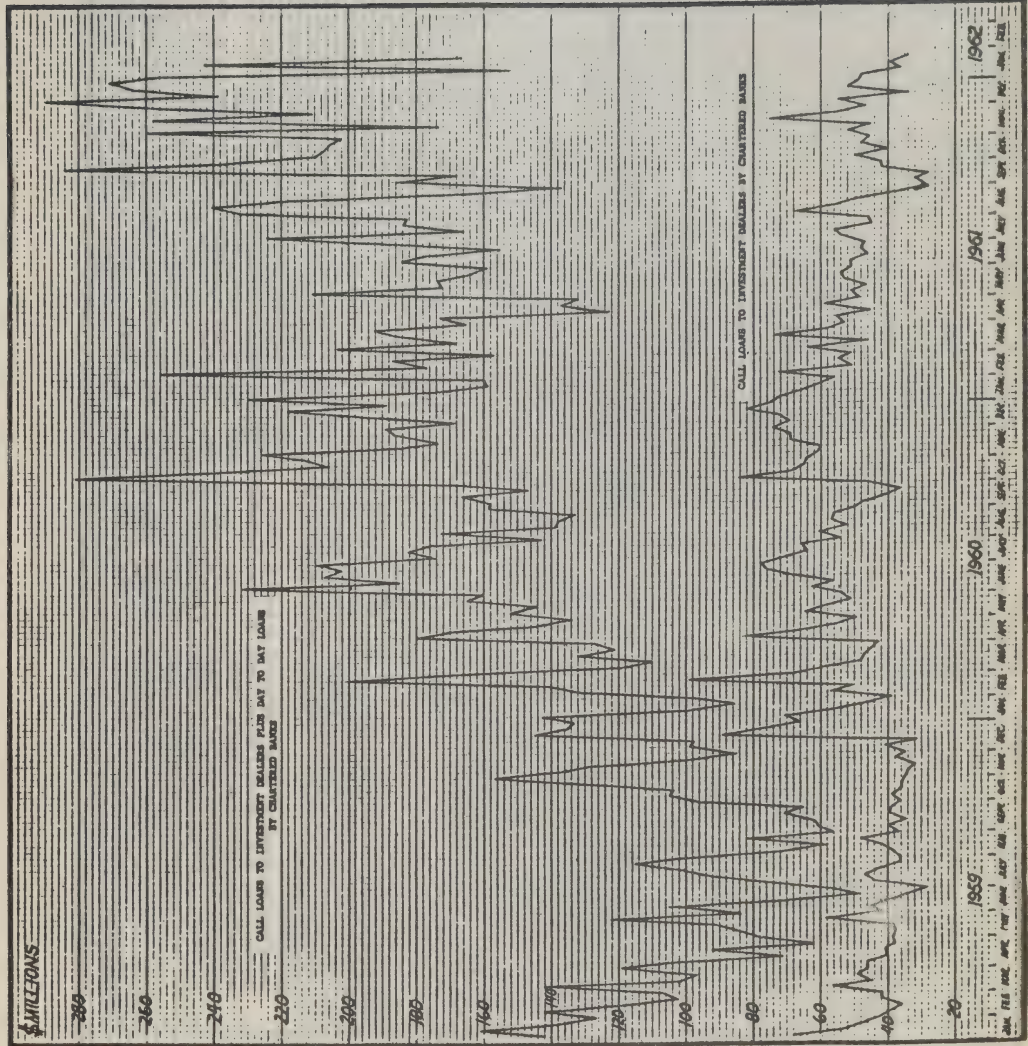
- 1
- 2 A. Graph 1 Investment Dealer Call Loans and Day
3 Loans placed with Chartered Banks
- 4 Graph 2 Investment Dealer Call Loans and Day
5 Loans placed with "Country Banks".
- 6 Graph 3 Investment Dealer Call Loans and Day
7 Loans -- Total
- 8 B. Revenue accruing to Chartered Banks
9 and other lenders from Call and Day
10 Loans
- 11 C. Table Changes Security Portfolios of Chartered
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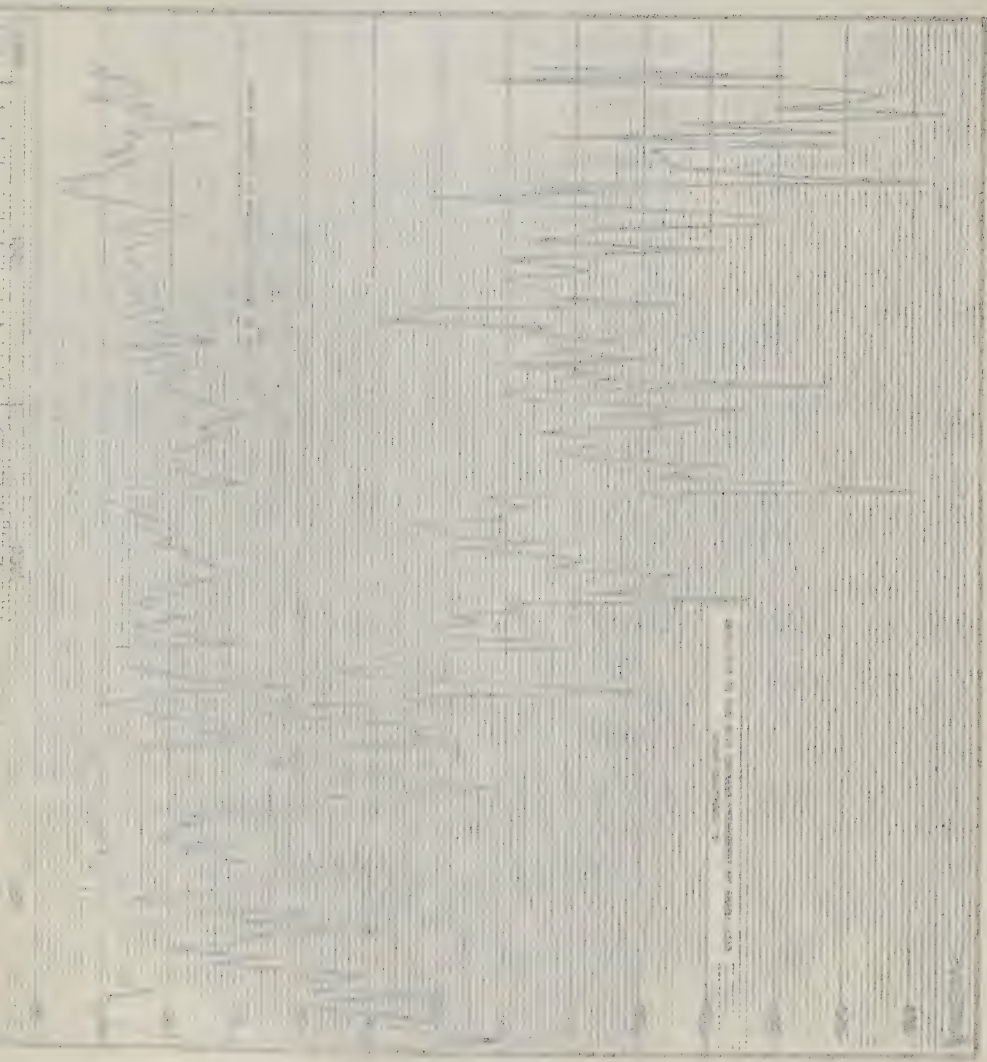


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Graph 2

LOANS OUTSIDE THE BANKING SYSTEM ARRANGED BY ANY METHOD ON THE COLLATERAL OF SECURITIES OWNED BY MEMBERS INCLUDING DAY-TO-DAY CALL AND TERM LOANS, BUY-BACK AND REPURCHASE AGREEMENTS WHERE THE AGGREGATE TOTAL OF SUCH BORROWING IS IN EXCESS OF \$500,000

\$ MILLIONS

Out

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Total of A B C and D:

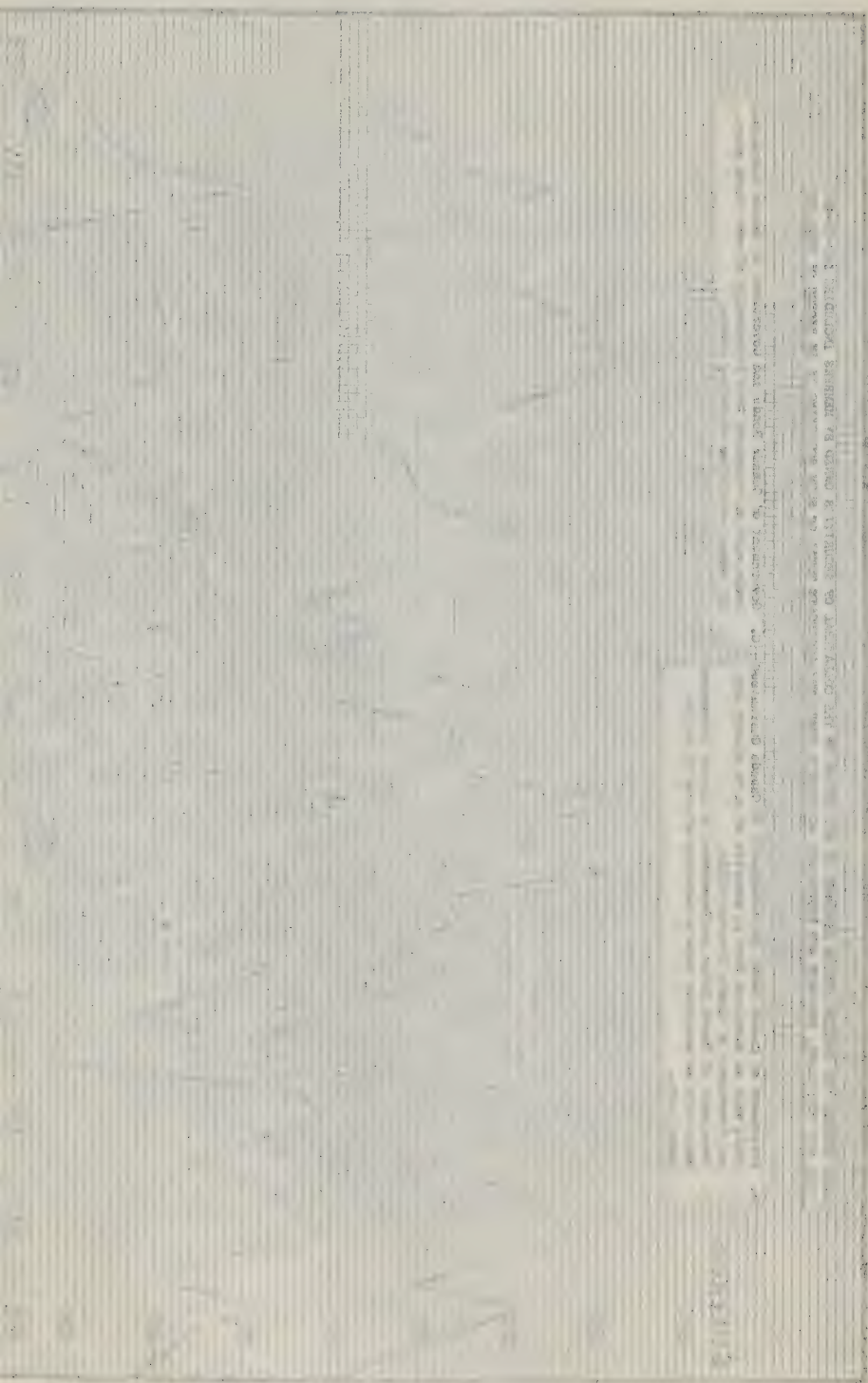
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FEB.		MAR.		APR.		MAY		JUNE		JULY		AUG.		SEPT.		OCT.		NOV.		DEC.		JAN.		FEB.		
8	15	1	8	15	22	29	5	12	19	26	3	10	17	24	31	7	14	21	28	4	11	18	25	1	8	15
9	16	2	9	16	23	30	6	13	20	27	4	11	18	25	1	8	15	22	29	5	12	19	26	3	10	
10	17	3	10	17	24	31	7	14	21	28	4	11	18	25	1	8	15	22	29	5	12	19	26	3	10	
11	18	4	11	18	25	1	8	15	22	29	5	12	19	26	3	10	17	24	31	7	14	21	28	4	11	
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15	22	8	15	22	29	5	12	19	26	3	10	17	24	31	7	14	21	28	4	11	18	25	1	8	15	
16	23	9	16	23	30	6	13	20	27	4	11	18	25	1	8	15	22	29	5	12	19	26	3	10	17	
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26		7	14	21	28	4	11	18	25	1	8	15	22	29	5	12	19	26	3	10	17	24	31			

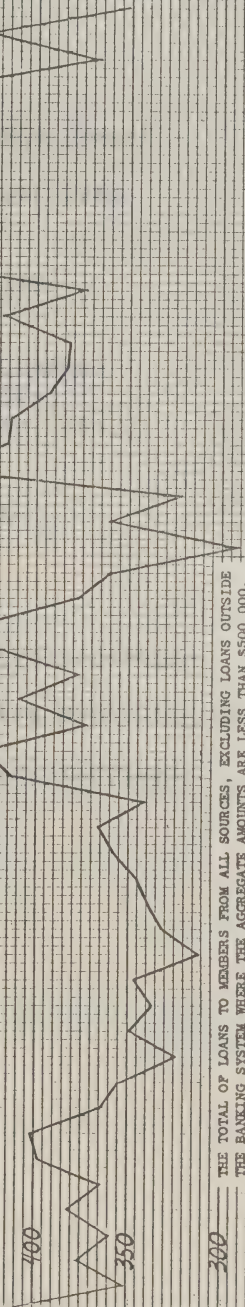


\$ MILLIONS
LOANS WITHIN THE CHARTERED BANKING SYSTEM AND LOANS OUTSIDE THE BANKING SYSTEM ARRANGED BY ANY METHOD ON THE COLLATERAL OF SECURITIES OWNED BY MEMBERS INCLUDING DAY-TO-DAY CALL AND TERM LOANS, BUY-BACK AND REPECHASE AGREEMENTS WHERE THE AGGREGATE TOTAL OF SUCH BORROWING IS IN EXCESS OF \$500,000.

500

450

400



300 THE TOTAL OF LOANS TO MEMBERS FROM ALL SOURCES, EXCLUDING LOANS OUTSIDE THE BANKING SYSTEM WHERE THE AGGREGATE AMOUNTS ARE LESS THAN \$500,000.

250

200

150

CALL LOANS PLUS DAY-TO-DAY LOANS TO MEMBERS MADE BY CHARTERED BANKS.

100

FEB. MAR. APR. MAY JUNE JULY AUG. SEPT. OCT. NOV. DEC. JAN. FEB.
8 15 22 1 8 15 22 29 5 12 19 26 3 10 17 24 31 7 14 21 28 5 12 19 26 2 9 16 23 30 6 13 20 27 4 11 18 25 1 8 15 22 29 6 13 20 27 3 10 17 24 31 7 14 21

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Nethercut & Young

Toronto, Ontario

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EXHIBIT B.

REVENUE ACCRUING TO CHARTERED BANKS AND OTHER
LENDERS FROM INTEREST ON LOANS, AND SERVICES
PROVIDED, TO MEMBERS OF THE INVESTMENT
DEALERS' ASSOCIATION OF CANADA - YEAR ENDED
DECEMBER 31, 1961

	<u>Chartered Banks</u>	<u>Other Lenders</u>
Interest on "Call Loans"	\$ 4,522,548	\$ 2,313,335
Interest on Short Term and Day Loans	3,656,621	3,225,230
Overcertification Charges	581,500	
Miscellaneous Charges (including drafts, delivery charges, etc.)	705,970	
TOTAL	\$ 9,466,639	\$ 5,538,565
Number of Members Reporting	186	186
Number of Members Reporting Nil	9	106
Number of Members Involved	177	80

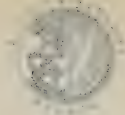


EXHIBIT B.

REVENUE ACCRUING TO CHARTERED BANKS AND OTHER
LENDERS FROM INTEREST ON LOANS, AND SERVICES
FURNISHED TO MEMBERS OF THE ASSOCIATION
DEALERS' ASSOCIATION OF CANADA - YEAR ENDED
DECEMBER 31, 1961

Other Lenders	Chartered Banks	
\$ 2,313,335	\$ 11,522,248	Interest on "Call Loans"
3,525,230	3,525,231	Interest on Short Term and Day Loans
	581,500	Overcollateralization Charges
	705,970	Miscellaneous Charges (including delivery charges, etc.)
\$ 5,838,565	\$ 9,466,639	TOTAL
186	186	Number of Members Reporting
106	9	Number of Members Reporting Nil
80	177	Number of Members Involved



EXHIBIT C

Type of Security	Net Issue or Retirement of Canadian Bonds and Stocks(3)					Net Increase or Decrease in Security Portfolios of Chartered Banks				
	1945	1946	1947	1948	1949	1945	1946	1947	1948	1949
Provincial	28*	18*	65	199	339	22	2	151	8	30 ^x
Municipal	43*	5*	31	71	89	15	24	18	7	21
Corporation	25	68	231	260	211	23	88	147	98	68 ^x
Total	46*	45	327	530	639	60	114	316	113	77 ^x

* Retirement
x Decrease

(3) Source: Appendix A, page 29. The table understates the total volume of net new issues of these securities in the Canadian market by the amount of the net reduction of foreign holdings of such securities through retirement or refunding.

Above from Bank of Canada Report 1949.

Wrote from Bank of Canada Report 1940.

securities through retirement or re-investing.

amount of the net redemption of foreign holdings of such
 net new issues of these securities in the Canadian market by the
 (3) source: Appendix A, page 80. The table indicates the total volume of

x Decrease
 * Retirement

	1940*	1941	1942	1943	1944	1945	1946	1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960
Total																					
Government																					
Municipal																					
Private																					
Total																					

Source: Bank of Canada, Report 1940, Appendix A, page 80.

Net Increase or Decrease in Securities

EXHIBIT C

1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30 31 32 33 34 35 36 37 38 39 40 41 42 43 44 45 46 47 48 49 50 51 52 53 54 55 56 57 58 59 60 61 62 63 64 65 66 67 68 69 70 71 72 73 74 75 76 77 78 79 80 81 82 83 84 85 86 87 88 89 90 91 92 93 94 95 96 97 98 99 100

EXHIBIT D
Table 2(a)

SELECTED CHARTERED BANK STATISTICS (000's omitted)

	1953	1952	1951	1950	1949	1948	1946
Gov't. of Can. Treas. Bills	244,000	235,000	285,000	132,000	126,000	194,000	1846
Gov't. of Can. Sec. Mat. 2 yrs.	482,000	489,000	489,000	334,000	783,000	139,000	147,000
Total	726,000	724,000	774,000	466,000	909,000	333,000	1,052,000
Gov't. of Can. Sec. Maturing after 2 years	2,032,774	1,777,217	2,019,211	2,266,122	2,223,556	2,027,698	2,117,535
Can. Provincial Securities	324,339	375,032	335,121	415,568	445,316	467,745	316,449
Can. Municipal Securities	151,690	155,971	167,470	131,704	161,262	139,935	115,462
Other Can. Securities	348,696	377,413	395,228	405,277	385,149	451,603	207,188
Total	2,955,082	2,700,021	3,673,428	4,093,500	4,102,490	3,603,118	3,936,304
Char. Banks Total Assets	10,722,306	10,135,350	9,609,602	9,495,936	8,718,138	7,973,986	7,798,628
Gov't. of Can. Treas. Bills						2,173,150	
% Char. Bank Total Assets	2.28	1.36	2.46	1.38	1.45	1.74	1.88
Gov't. of Can. Sec. Mat. 2 yrs.						7.73	15.38
% Char. Bank Total Assets	6.77	9.31	7.64	8.66	10.19	9.16	
Gov't. of Can. Sec. Mat. after 2 years						15.43	27.15
% Char. Bank Total Assets	18.97	17.50	21.01	23.76	25.50	25.33	
Can. Prov. Securities % Char. Bank						5.87	4.06
Total Assets	3.19	3.73	3.70	4.32	5.11	9.54	
Can. Mun. Securities % Char. Bank						1.63	1.43
Total Assets	1.42	1.57	1.74	2.04	1.85	1.67	
Other Can. Securities % Char. Bank						4.44	2.56
Total Assets	3.25	3.72	4.16	4.27	4.40	4.44	
Gov't. of Can. Treas. Bills & Sec. Mat. within 2 yrs. % Char. Banks Total Assets	33.53	36.43	38.25	43.11	47.06	45.19	50.73
Char. Banks Holdings of all Sec. except Treas. Bills and Canadian Mat. under 2 years	2,868,689	2,633,059	2,940,898	2,270,749	3,213,883	2,982,590	2,756,654
Char. Banks Holdings of all Sec. + Mfgs. except Treas. Bills & Cdn. Mat. under 2 years	2,869,098	2,633,508	2,941,284	2,271,205	3,214,333	2,983,808	2,759,302
Char. Banks Holdings of all Secs. + Mfgs. except Treas. Bills and Cdn. Mat. under 2 yrs. % Pers. Sav. Dep.	54.99	54.70	63.78	71.76	72.50	79.77	79.51
Personal Savings Deposits	5,034,050	4,994,469	4,611,594	4,558,417	4,433,352	4,056,953	3,740,442
Demand Deposits	3,180,050	3,242,094	2,952,711	2,770,388	2,770,427	2,289,585	2,280,809
Other Deposits	849,713	412,493	481,433	616,622	463,462	464,018	404,874
Total Deposits	9,063,813	8,579,076	8,045,668	7,945,427	7,722,291	6,440,901	6,276,733
Char. Banks Holdings of all Sec. except Treas. Bills & Cdn. Mat. under 2 yrs. % Pers. Sav. Dep.	56.99	54.69	63.77	71.73	72.49	79.87	79.46
Char. Banks Holdings of all Sec. except Treas. Bills & Cdn. Mat. under 2 yrs. % Demand Deposits	90.21	83.07	99.26	118.06	132.44	129.93	120.34
Char. Banks Holdings of all Sec. except Treas. Bills & Cdn. Mat. under 2 yrs. % Total Deposits	31.65	31.39	34.31	41.17	43.90	43.87	43.92
Char. Banks Holdings of all Secs. + Mfg. except Treas. Bills & Cdn. Mat. under 2 yrs. % Total Deposits	31.66	31.40	36.31	41.17	43.90	43.88	43.94

B. & O. E.

EXHIBIT D
Table 2(b)

— 40 —



EXHIBIT "E"

EXCERPT FROM THE BANK OF CANADA ANNUAL REPORT 1956

THE BANKING SYSTEM

1. One reason why it is not possible to predict the effects of monetary measures with accuracy is the uncertainty, which must always exist to some degree, as to the reaction of the banking system itself to such measures. In Canada this has been more noticeable perhaps than elsewhere because of the extent to which commercial banking functions and savings banking functions are intermingled in the operations of the chartered banks. Over 80 per cent of total personal savings deposits in Canada are held with the chartered banks, and the pattern of investment of such deposits has varied widely at different times. The banks may under conditions of inflationary pressure expand their commercial and general loans and other forms of short-term credit from such funds, which in other times would go into long-term investments, including (since 1954) housing loans. This has happened in each of the postwar credit expansion cycles (1947-48, 1950-51, 1952-53 and 1955-56).

2. The possibility of such a development has made it necessary for the central bank to regard the total volume of deposits of the chartered banks, including personal savings deposits, as forming part of the money supply, whereas the savings deposits held with specialized savings institutions (e.g. trust companies, loan companies, savings banks, credit unions) are not so regarded. At a time of strong demand for short-term credit, therefore, the central bank must endeavour to restrain any increase



EXHIBIT "F"

EXCERPT FROM THE BANK OF CANADA ANNUAL REPORT 1956

THE BANKING SYSTEM

1. One reason why it is not possible to predict the effects of monetary measures with accuracy is the uncertainty, which must always exist to some degree, as to the reaction of the banking system itself to such measures. In Canada this has been more noticeable perhaps than elsewhere because of the extent to which commercial banks are intermingled in the operations of the chartered banks. Over 80 per cent of total personal savings deposits in Canada are held with the chartered banks, and the pattern of investment of such deposits has varied widely at different times. The banks may under conditions of inflationary pressure expand their commercial and general loans and other forms of short-term credit from such funds, which in other times would go into long-term investments, including (since 1954) housing loans. This has happened in each of the postwar credit expansion cycles (1947-48, 1950-51, 1952-53 and 1955-56).

2. The possibility of such a development has made it necessary for the central bank to regard the total volume of deposits of the chartered banks, including personal savings deposits, as forming part of the money supply, whereas the savings deposits held with specialist savings institutions (e.g. trust companies, loan companies, savings banks, credit unions) are not so regarded. At a time of strong demand for short-term credit, therefore, the central bank must endeavour to restrain any increase



1 in total bank deposits, to such a degree that the natural
2 and virtually unavoidable increase in personal savings
3 deposits is largely or at times entirely matched by a
4 decline in other deposits.

5 3. Even so, the effects on credit expansion of
6 any particular degree of restraint on monetary expansion
7 cannot be predicted with confidence, because of the
8 availability for commercial and general loans of funds
9 that can be obtained by the banks by selling in large
10 volume the Government securities in which a considerable
11 proportion of their savings deposits had previously
12 been invested. By this means, the greater part of the
13 resources of the banks' savings departments have been
14 available as required from time to time to augment the
15 other resources of the banks' commercial banking
16 departments when the demand for commercial loans has been
17 particularly great. Housing loans and other
18 investments have been the residual form of investment for
19 the savings departments of the banks.

20 4. In other countries personal savings deposits
21 are chiefly held by separate and specialized institutions,
22 sometimes called building societies, sometimes called
23 savings and loan associations, sometimes called savings
24 banks or mutual savings banks, which make a practice of
25 investing such funds in housing loans and in relatively
26 long-term securities. Their objective is to invest to
27 the best advantage in order to obtain the largest revenue
28 consistent with prudent investment practices, and in
29 order thereby to be able to pay the highest possible
30 rate of interest to their depositors. Experience has



in total bank deposits, to such a degree that the national
deposits is largely or at times entirely matched by a
decline in other deposits.
3. Even so, the effects on credit expansion of
any particular degree of restraint on monetary expansion
cannot be predicted with confidence, because of the
availability for commercial and general loans of funds
that can be obtained by the banks by selling in large
volume the Government securities in which a considerable
part of their assets have been invested. By this means, the greatest part of the
available as required from time to time to augment the
other resources of the banks, commercial banking
departments when the demand for commercial loans has been
particularly great. Housing loans and other
investments have been the residual form of investment for
the savings departments of the banks.
4. In other countries personal savings deposits
are chiefly held by separate and specialized institutions
sometimes called building societies, sometimes called
savings and loan associations, sometimes called savings
banks or mutual savings banks, which make a practice of
long-term securities. Their objective is to invest in
the best advantage in order to obtain the largest revenue
consistent with prudent investment practices, and in
order thereby to be able to pay the highest possible
rate of interest to their depositors. Experience has



1 shown that rarely if ever does a savings institution
2 encounter an actual decline in its total volume of
3 deposits, other than purely temporary or seasonal
4 fluctuations which a reasonable degree of liquidity in
5 its assets will permit it to meet without having to run
6 the risk of losses through sales of long-term investments
7 prior to maturity. The great bulk of personal savings
8 deposits, increasing from year to year, are accordingly
9 invested in non-commercial-banking types of loans and
10 investments, and the central bank does not regard such
11 deposits as part of the supply of "money" that need be
12 directly influenced by monetary operations.

13 5. The different evolution of the Canadian banking
14 structure has created problems relating both to
15 fluctuations in short-term credit and to fluctuations in
16 long-term investment. Until 1954 the Canadian
17 chartered banks were not permitted by law to lend money
18 on housing or other forms of real estate, presumably
19 because they were primarily regarded as commercial banks.
20 Because of their efficient operation of a widespread
21 branch system in a large sparsely settled country they
22 managed to attract most of the personal savings
23 deposits of the people, and these became increasingly
24 important as the country developed. The increase in
25 the chartered banks' savings deposits has averaged
26 \$340 million a year over the last five years and will
27 no doubt continue to rise in the future. Specialized
28 savings institutions grew much more slowly, and mainly
29 in the large cities. The kind of investments such
30 institutions might have made were for the most part not

...that rarely if ever does a savings institution
encounter an actual decline in its total volume of

...which a reasonable degree of liquidity in
its assets will permit it to meet without having to run
the risk of losses through sales of long-term investments
prior to maturity. The great bulk of personal savings
deposits, increasing from year to year, are accordingly
invested in non-commercial-banking types of loans and
deposits as part of the supply of "money" that need be
directly influenced by monetary operations.

5. The different evolution of the Canadian banking
structure has created problems relating both to
liquidity in short-term credit and to investments in
long-term investment. Until 1925 the Canadian
chartered banks were not permitted by law to lend money
on housing or other forms of real estate, presumably
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1 made by the chartered banks.

2 6. In 1954 the Bank Act was amended to permit the
3 chartered banks to make mortgage loans on new houses,
4 loans insured under the National Housing Act. This was
5 an important improvement in the machinery of the
6 Canadian capital market. I believe it would be
7 desirable if means could now be found to encourage
8 greater stability in the rate of long-term investment
9 by the banks in those fields where they may now operate.

10 7. It may be that specialized savings institutions,
11 which invest their fund in housing loans and other long-
12 term investments and are able thereby to pay higher
13 rates of interest on savings deposits than the chartered
14 banks, will grow in importance and attract a growing
15 part of the future personal savings of Canadians. To
16 maintain their relative position, the chartered banks
17 may find it desirable and necessary to operate in respect
18 of the resources of their savings departments in much
19 the same way as a savings bank and use such resources
20 to provide funds for the kinds of investment naturally
21 associated with long-term savings.

22 8. To the extent that personal savings were
23 segregated from the commercial lending field, they
24 could be regarded as likewise removed from the category
25 of "money supply". The banks' short-term credit
26 operations would become more responsive to changes in
27 monetary conditions. It would, of course, be the duty
28 of the central bank -- as it is today -- to see that
29 sufficient money was made available to permit an adequate
30 volume of short-term credit to be provided through the

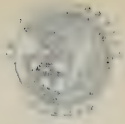


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1 banking system. The volume of short-term loans might
2 not be any different from what it has been, on the
3 average and allowing for normal growth, but a tendency
4 towards excessive expansion in periods of inflationary
5 pressures would be more readily restrained. Fluctuations
6 in mortgage lending would of course be much less
7 pronounced. The workings of monetary policy would
8 become more predictable and more effective. The
9 possibility of a gradual approach towards arrangements
10 of the sort outlined would seem to be worthy of study
11 and discussion. Progress in such an approach would be
12 directed towards expanding mortgage loans and other
13 appropriate investments based on future increases in
14 savings deposits, not reducing the volume of commercial
15 or general loans.

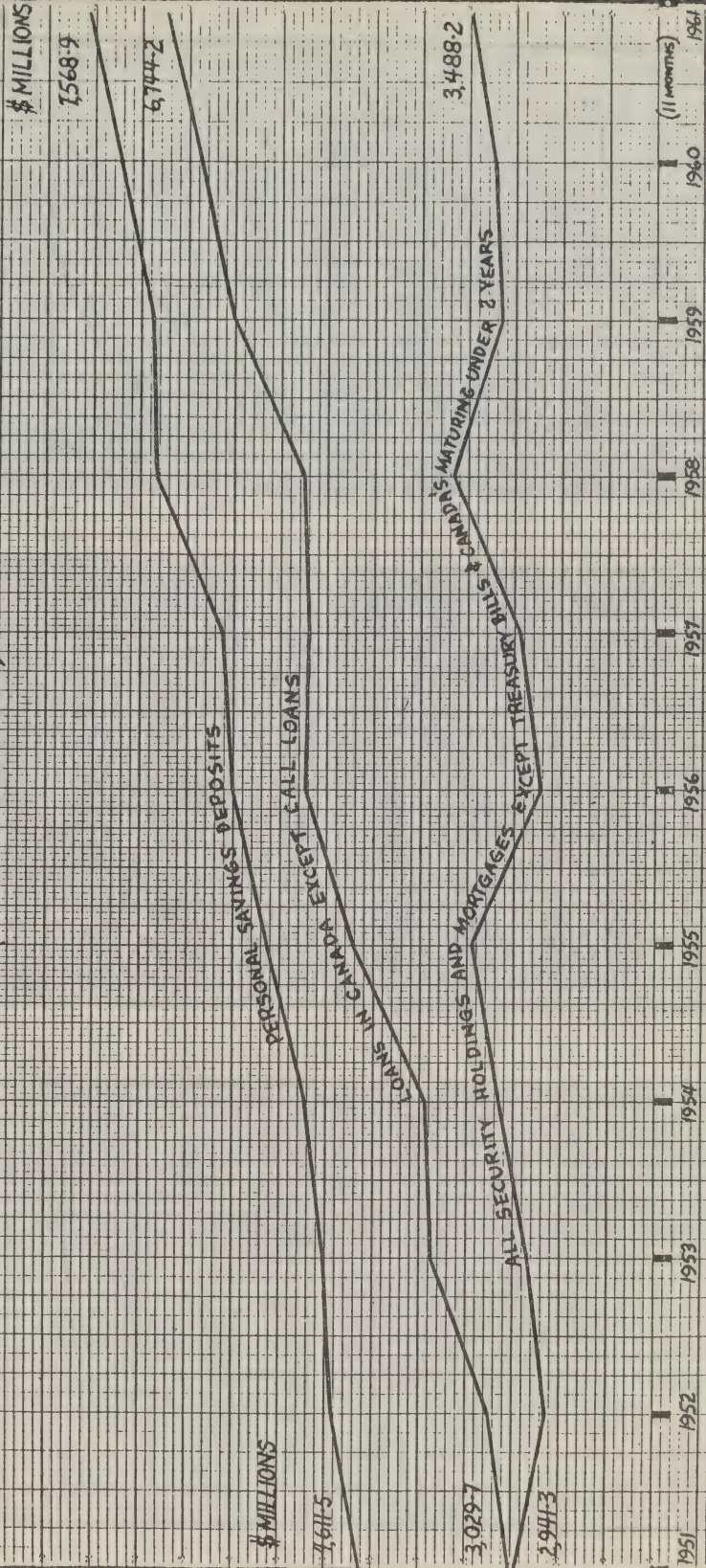
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17 Bank of Canada Annual Report 1956 (pages 27-31).
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Bank of Canada Annual Report 1956 (pages 27-31):

CANADIAN CHARTERED BANKS (AS AT DECEMBER 31ST)



(11 months)

1880

WATERWAY OF THE NORTH RIVER

1880

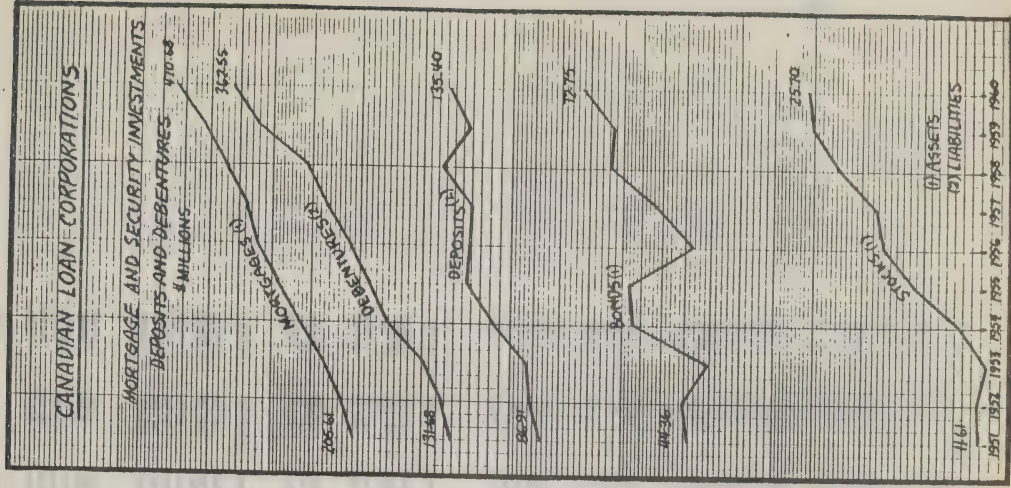
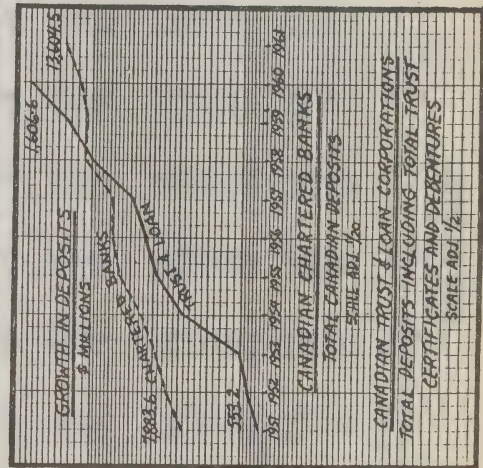
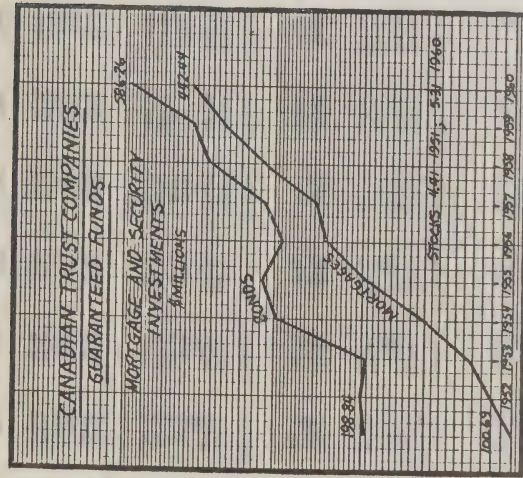
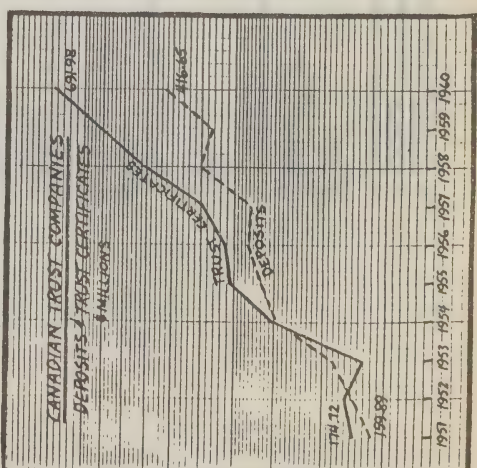
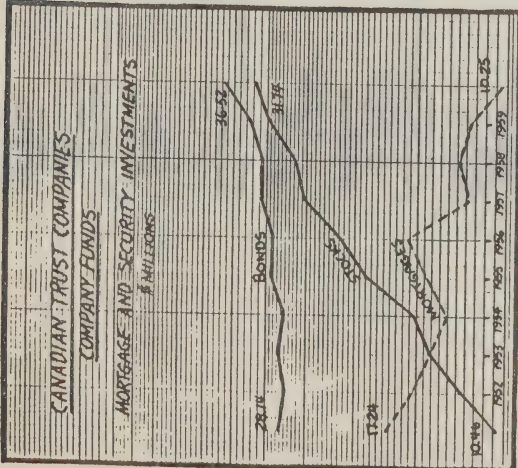
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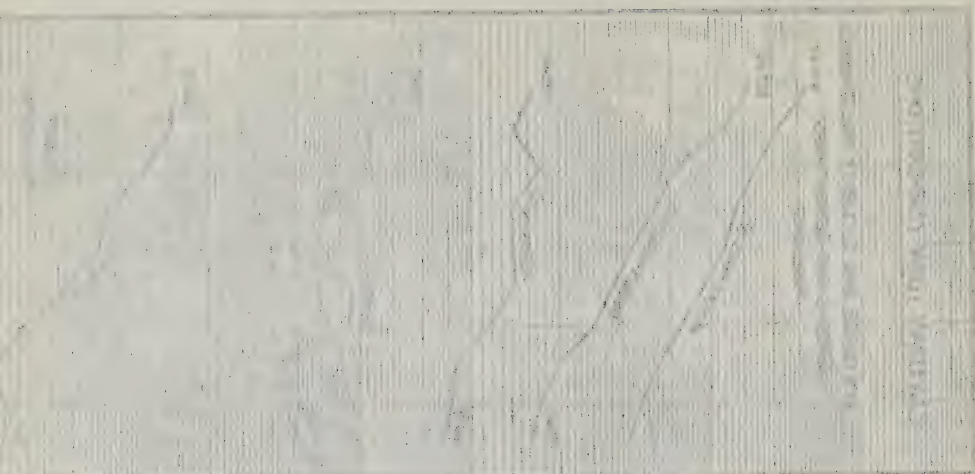


EXHIBIT C
Table 1

CANADIAN TRUST COMPANIES (as at December 31st.)

Balance Sheet (\$ millions)	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	2038	2039	2040	2041	2042	2043	2044	2045	2046	2047	2048	2049	2050	2051	2052	2053	2054	2055	2056	2057	2058	2059	2060	2061	2062	2063	2064	2065	2066	2067	2068	2069	2070	2071	2072	2073	2074	2075	2076	2077	2078	2079	2080	2081	2082	2083	2084	2085	2086	2087	2088	2089	2090	2091	2092	2093	2094	2095	2096	2097	2098	2099	2100	2101	2102	2103	2104	2105	2106	2107	2108	2109	2110	2111	2112	2113	2114	2115	2116	2117	2118	2119	2120	2121	2122	2123	2124	2125	2126	2127	2128	2129	2130	2131	2132	2133	2134	2135	2136	2137	2138	2139	2140	2141	2142	2143	2144	2145	2146	2147	2148	2149	2150	2151	2152	2153	2154	2155	2156	2157	2158	2159	2160	2161	2162	2163	2164	2165	2166	2167	2168	2169	2170	2171	2172	2173	2174	2175	2176	2177	2178	2179	2180	2181	2182	2183	2184	2185	2186	2187	2188	2189	2190	2191	2192	2193	2194	2195	2196	2197	2198	2199	2200	2201	2202	2203	2204	2205	2206	2207	2208	2209	2210	2211	2212	2213	2214	2215	2216	2217	2218	2219	2220	2221	2222	2223	2224	2225	2226	2227	2228	2229	2230	2231	2232	2233	2234	2235	2236	2237	2238	2239	2240	2241	2242	2243	2244	2245	2246	2247	2248	2249	2250	2251	2252	2253	2254	2255	2256	2257	2258	2259	2260	2261	2262	2263	2264	2265	2266	2267	2268	2269	2270	2271	2272	2273	2274	2275	2276	2277	2278	2279	2280	2281	2282	2283	2284	2285	2286	2287	2288	2289	2290	2291	2292	2293	2294	2295	2296	2297	2298	2299	2300	2301	2302	2303	2304	2305	2306	2307	2308	2309	2310	2311	2312	2313	2314	2315	2316	2317	2318	2319	2320	2321	2322	2323	2324	2325	2326	2327	2328	2329	2330	2331	2332	2333	2334	2335	2336	2337	2338	2339	2340	2341	2342	2343	2344	2345	2346	2347	2348	2349	2350	2351	2352	2353	2354	2355	2356	2357	2358	2359	2360	2361	2362	2363	2364	2365	2366	2367	2368	2369	2370	2371	2372	2373	2374	2375	2376	2377	2378	2379	2380	2381	2382	2383	2384	2385	2386	2387	2388	2389	2390	2391	2392	2393	2394	2395	2396	2397	2398	2399	2400	2401	2402	2403	2404	2405	2406	2407	2408	2409	2410	2411	2412	2413	2414	2415	2416	2417	2418	2419	2420	2421	2422	2423	2424	2425	2426	2427	2428	2429	2430	2431	2432	2433	2434	2435	2436	2437	2438	2439	2440	2441	2442	2443	2444	2445	2446	2447	2448	2449	2450	2451	2452	2453	2454	2455	2456	2457	2458	2459	2460	2461	2462	2463	2464	2465	2466	2467	2468	2469	2470	2471	2472	2473	2474	2475	2476	2477	2478	2479	2480	2481	2482	2483	2484	2485	2486	2487	2488	2489	2490	2491	2492	2493	2494	2495	2496	2497	2498	2499	2500	2501	2502	2503	2504	2505	2506	2507	2508	2509	2510	2511	2512	2513	2514	2515	2516	2517	2518	2519	2520	2521	2522	2523	2524	2525	2526	2527	2528	2529	2530	2531	2532	2533	2534	2535	2536	2537	2538	2539	2540	2541	2542	2543	2544	2545	2546	2547	2548	2549	2550	2551	2552	2553	2554	2555	2556	2557	2558	2559	2560	2561	2562	2563	2564	2565	2566	2567	2568	2569	2570	2571	2572	2573	2574	2575	2576	2577	2578	2579	2580	2581	2582	2583	2584	2585	2586	2587	2588	2589	2590	2591	2592	2593	2594	2595	2596	2597	2598	2599	2600	2601	2602	2603	2604	2605	2606	2607	2608	2609	2610	2611	2612	2613	2614	2615	2616	2617	2618	2619	2620	2621	2622	2623	2624	2625	2626	2627	2628	2629	2630	2631	2632	2633	2634	2635	2636	2637	2638	2639	2640	2641	2642	2643	2644	2645	2646	2647	2648	2649	2650	2651	2652	2653	2654	2655	2656	2657	2658	2659	2660	2661	2662	2663	2664	2665	2666	2667	2668	2669	2670	2671	2672	2673	2674	2675	2676	2677	2678	2679	2680	2681	2682	2683	2684	2685	2686	2687	2688	2689	2690	2691	2692	2693	2694	2695	2696	2697	2698	2699	2700	2701	2702	2703	2704	2705	2706	2707	2708	2709	2710	2711	2712	2713	2714	2715	2716	2717	2718	2719	2720	2721	2722	2723	2724	2725	2726	2727	2728	2729	2730	2731	2732	2733	2734	2735	2736	2737	2738	2739	2740	2741	2742	2743	2744	2745	2746	2747	2748	2749	2750	2751	2752	2753	2754	2755	2756	2757	2758	2759	2760	2761	2762	2763	2764	2765	2766	2767	2768	2769	2770	2771	2772	2773	2774	2775	2776	2777	2778	2779	2780	2781	2782	2783	2784	2785	2786	2787	2788	2789	2790	2791	2792	2793	2794	2795	2796	2797	2798	2799	2800	2801	2802	2803	2804	2805	2806	2807	2808	2809	2810	2811	2812	2813	2814	2815	2816	2817	2818	2819	2820	2821	2822	2823	2824	2825	2826	2827	2828	2829	2830	2831	2832	2833	2834	2835	2836	2837	2838	2839	2840	2841	2842	2843	2844	2845	2846	2847	2848	2849	2850	2851	2852	2853	2854	2855	2856	2857	2858	2859	2860	2861	2862	2863	2864	2865	2866	2867	2868	2869	2870	2871	2872	2873	2874	2875	2876	2877	2878	2879	2880	2881	2882	2883	2884	2885	2886	2887	2888	2889	2890	2891	2892	2893	2894	2895	2896	2897	2898	2899	2900	2901	2902	2903	2904	2905	2906	2907	2908	2909	2910	2911	2912	2913	2914	2915	2916	2917	2918	2919	2920	2921	2922	2923	2924	2925	2926	2927	2928	2929	2930	2931	2932	2933	2934	2935	2936	2937	2938	2939	2940	2941	2942	2943	2944	2945	2946	2947	2948	2949	2950	2951	2952	2953	2954	2955	2956	2957	2958	2959	2960	2961	2962	2963	2964	2965	2966	2967	2968	2969	2970	2971	2972	2973	2974	2975	2976	2977	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Table 2
EXHIBIT G
CANADIAN TRUST COMPANIES (as at December 31st)

Ratios	1960	1959	1958	1957	1956	1955	1954	1953	1952	1951
Guaranteed Fund % Total Assets	90.57	89.20	88.75	86.56	86.30	86.80	86.15	81.94	82.24	81.33
Guaranteed Fund Mortgages % Total Guar. Fund Assets	39.85	42.37	39.26	39.30	39.87	34.55	30.16	34.44	31.23	30.03
Guaranteed Fund Securities % Total Guaranteed Fund Assets	53.28	49.14	51.04	50.47	49.42	55.80	59.86	55.71	57.27	60.62
Deposits % Guaranteed Funds	37.52	37.53	43.46	44.33	47.18	46.21	49.40	53.39	49.10	47.69
Equity % Guaranteed Funds	9.01	10.59	10.96	13.37	13.54	12.97	13.46	18.58	18.27	19.15
Company Fund Mortgages % Total Company Fund Assets	8.87	10.86	12.18	12.21	16.62	16.44	16.19	17.91	19.88	22.40
Company Fund Securities % Total Company Fund Assets	59.06	57.01	55.99	57.50	53.25	54.84	53.03	53.89	52.13	50.16
Revenue from Estates, Trusts, etc. % Total under Administration	0.53	0.53	0.54	0.57	0.56	0.55	0.51	0.50	0.48	0.47
Profit in Guaranteed Funds % Total Assets Guar. Fund	1.32	1.31	1.28	1.37	1.37	1.37	1.28	1.55	1.48	1.38
Company Fund Mortgage Rev. % Mortgage Investment	8.98	7.26	7.47	7.80	6.35	5.41	6.24	5.92	6.23	5.28
Company Fund Securities Rev. % Securities Investment	5.70	5.82	6.18	4.82	5.54	5.19	5.35	4.43	4.85	5.41
Company Fund Revenues % Company Fund Assets	6.45	6.05	6.29	5.59	5.65	5.29	5.41	4.96	5.08	5.20
Expenditures % Revenue	74.12	74.37	74.85	75.81	74.85	73.73	73.30	74.84	N.A.	N.A.
Net Profit % Equity	8.28	8.03	5.69	5.37	4.93	7.38	7.00	6.24	5.46	5.11
Dividend % Net Profit	60.39	58.75	57.24	62.60	57.17	57.50	60.50	66.91	77.68	82.32

* Borrowing power on debentures and other securities and by way of deposits, by law, is limited to 1½ times (8%) of Paid-up Capital and Reserve (equity).

Source: Report of the Registrar of Loan and Trust Corporations for the Province of Ontario. The report includes the particulars of the business of each trust company registered and conducting business in Ontario comprised of the following twenty-three companies in 1960, listed in order of size of total assets, including estates, trusts and agency funds under administration, in \$ millions.

- | | | | | | |
|---------------------------------|----------|----------------------------------|--------|------------------------------------|-------|
| 1. Royal Trust Co. | 2,461.83 | 9. Guaranty Trust Co. | 249.83 | 17. Premier Trust Co. | 28.96 |
| 2. Montreal Trust Co. | 1,817.03 | 10. Crown Trust Co. | 240.08 | 18. Prudential Trust Co. | 21.24 |
| 3. National Trust Co. | 837.80 | 11. Canada Permanent Trust Co. | 205.91 | 19. Industrial Mortgage & Tr. Co. | 20.94 |
| 4. Toronto General Trusts Corp. | 607.85 | 12. Chartered Trust Co. | 182.48 | 20. Investors Trust Co. | 13.95 |
| 5. Canada Trust Co. | 491.20 | 13. Waterloo Trust & Savings Co. | 110.37 | 21. Hulton & Peel Trust & Sav. Co. | 12.35 |
| 6. Administration and Trust Co. | 301.89 | 14. Victoria and Grey Trust Co. | 99.33 | 22. Lambton Trust Co. | 3.83 |
| 7. Eastern Trust Co. | 254.78 | 15. British Mortgage & Trust Co. | 44.72 | 23. Bankers' Trust Co. | .43 |
| 8. General Trust of Canada | 252.03 | 16. Sterling Trusts Corp. | 35.96 | | |

CANADIAN TRUST COMPANIES

[illegible]

	Industry (23 com.)	Chartered Trust	Crown Trust	Eastern Trust	Guaranty Trust	Industrial Trust	National Trust	Premier Trust	Royal Trust	Victoria & Waterloo Trust
Assets (\$ millions)										
Assets, Funds	10.25	.08	—	1.05	—	.23	.80	.40	1.67	—
- Mortgages	36.32	3.15	2.06	1.50	4.37	3.4	2.61	1.14	5.04	.44
- Bonds	31.74	.86	.83	.76	1.99	.10	4.86	.11	3.78	1.83
Total Co. Fund Assets	115.57	5.50	4.17	4.23	8.23	1.43	13.23	2.06	22.25	4.40
Guaranteed Funds										
- Mortgages	442.44	22.40	21.60	16.49	45.27	8.84	25.03	15.07	23.99	43.01
- Bonds	586.26	21.13	13.03	22.04	43.30	5.67	52.01	2.79	133.74	32.54
- Stocks	5.21	—	.06	.36	.11	.11	—	—	—	—
Total Guar. Fund Assets	1,100.21	44.73	37.04	41.25	94.87	15.15	129.54	18.68	186.43	71.51
Grand Total Assets	1,225.89	50.23	41.21	45.51	109.10	16.57	142.83	21.72	209.68	70.16
Estates, Trusts & Agency Funds	7,068.80	132.26	194.87	209.27	146.73	4.37	1,674.21	7.24	2,232.15	21.65
Liabilities (\$ millions)										
Company Funds	100.06	4.31	4.01	3.20	7.51	1.35	11.84	1.94	16.23	5.19
- Equity										4.20
Guaranteed Funds										
- Deposits	416.85	24.56	17.85	10.36	47.14	6.78	10.07	3.07	—	22.42
- Trust Certificates	681.26	17.60	13.09	30.80	47.73	8.37	112.46	14.59	186.37	49.37
Revenue (\$ millions)										
Estates, Trusts etc.	37.17	1.66	2.06	1.12	1.43	.02	8.59	.12	8.98	.10
Profit in Guar. Fund	14.62	.72	.70	.48	1.36	.28	1.20	.56	1.33	1.12
Company Funds	—	—	—	—	—	—	—	—	—	—
- Mortgages	.82	.01	—	.07	—	.03	.06	.04	.10	.01
- Bonds (1)	1.81	.14	.10	.08	.22	.10	.08	.07	.23	.06
- Stocks (1)	1.70	.04	.04	.03	.09	.04	.25	.02	.27	.09
(1) Includes net profit on sale of securities.										
Total Revenue	49.26	2.82	2.04	1.76	3.20	.37	8.71	.81	11.62	1.84
Net Income	21.25	2.13	2.43	1.40	1.82	.23	6.37	.59	8.77	1.04
Net Earnings before Taxes	15.33	1.72	1.83	1.03	1.35	.14	5.41	.41	8.19	.93
Income Taxes	7.05	.45	.28	.19	.60	.06	.85	.29	1.33	.35
Net Profit	8.28	.27	.33	.21	.73	.08	1.18	.64	1.52	.47
Dividends	5.00	.18	.15	.14	.28	.07	.69	.10	.96	.18
Ratio										
Co. Assets, & Co. Fund Assets	8.57	.35	—	24.82	—	15.20	6.77	13.42	7.16	3.24
Co. Bonds & Co. Fund Assets	31.60	57.27	49.48	35.46	53.10	23.94	31.11	20.96	35.31	23.18
Co. Stocks & Co. Fund Assets	27.46	17.82	23.20	17.87	24.18	7.04	37.50	8.34	23.74	64.40
Guar. Mgt. & Guar. Fund Assets	39.85	50.09	58.32	33.95	47.72	56.35	19.32	32.87	76.65	59.89
Guar. Bonds & Guar. Fund Assets	52.80	47.25	35.18	53.39	45.54	37.43	71.49	37.01	14.19	49.48
Guar. Fund & Grand Total Assets	80.37	89.05	49.48	90.71	92.02	91.43	90.70	90.32	98.41	93.73
Deposits & Guar. Fund	37.23	39.38	48.46	23.15	49.69	44.75	8.23	86.95	13.62	31.22
Trust Certs. & Guar. Fund	32.32	39.80	51.54	74.85	50.31	55.25	91.77	13.05	84.38	59.97
Equity & Guar. Fund	9.01	10.08	10.83	7.75	7.82	8.91	9.22	9.87	8.72	6.39
Revenue from Estates etc. & Profit in Guar. Funds & Total	.53	1.41	1.04	.54	.97	.46	.39	1.66	.40	.72
Income Yield on Co. Mgt. & (2)	1.32	1.61	1.89	1.16	1.43	1.85	2.85	1.85	.72	1.83
Income Yield on Co. Bonds (2)	8.98	—	—	6.67	—	13.04	6.67	—	11.06	5.99
Income Yield on Co. Stocks (2)	4.96	4.44	4.21	3.33	5.03	2.94	3.20	2.63	6.55	9.09
Income Yield on Co. Funds (2)	1.36	4.06	4.30	3.85	4.53	4.65	5.02	7.04	18.98	6.35
Income Yield on Co. Assets (2)	1.80	1.91	2.28	1.41	1.73	2.11	1.48	2.00	3.18	2.24
Expenditures & Revenue	74.12	74.47	79.53	79.53	94.88	63.16	75.43	49.38	75.47	56.52
Net Profit & Grand Total Assets	.68	.74	.80	.46	.76	.48	.83	.53	.97	.61
Net Profit & Equity	8.28	8.20	8.23	6.56	10.39	5.53	9.97	8.90	10.82	9.08
Dividend & Net Profit	60.38	46.63	45.45	66.67	35.90	67.30	37.96	47.62	63.16	72.34

(2) Calculated on 1960 revenues as a percentage of book value of mortgage and security investments outstanding as at December 31st, 1960 and is, therefore, not a weighted average return on investment.

CANADIAN LOAN CORPORATION (as at December 31st)

EXHIBIT C
Table 5

Balance Sheet (\$ millions)

	1960	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036	2037	2038	2039	2040	2041	2042	2043	2044	2045	2046	2047	2048	2049	2050	2051	2052	2053	2054	2055	2056	2057	2058	2059	2060	2061	2062	2063	2064	2065	2066	2067	2068	2069	2070	2071	2072	2073	2074	2075	2076	2077	2078	2079	2080	2081	2082	2083	2084	2085	2086	2087	2088	2089	2090	2091	2092	2093	2094	2095	2096	2097	2098	2099	2100	2101	2102	2103	2104	2105	2106	2107	2108	2109	2110	2111	2112	2113	2114	2115	2116	2117	2118	2119	2120	2121	2122	2123	2124	2125	2126	2127	2128	2129	2130	2131	2132	2133	2134	2135	2136	2137	2138	2139	2140	2141	2142	2143	2144	2145	2146	2147	2148	2149	2150	2151	2152	2153	2154	2155	2156	2157	2158	2159	2160	2161	2162	2163	2164	2165	2166	2167	2168	2169	2170	2171	2172	2173	2174	2175	2176	2177	2178	2179	2180	2181	2182	2183	2184	2185	2186	2187	2188	2189	2190	2191	2192	2193	2194	2195	2196	2197	2198	2199	2200	2201	2202	2203	2204	2205	2206	2207	2208	2209	2210	2211	2212	2213	2214	2215	2216	2217	2218	2219	2220	2221	2222	2223	2224	2225	2226	2227	2228	2229	2230	2231	2232	2233	2234	2235	2236	2237	2238	2239	2240	2241	2242	2243	2244	2245	2246	2247	2248	2249	2250	2251	2252	2253	2254	2255	2256	2257	2258	2259	2260	2261	2262	2263	2264	2265	2266	2267	2268	2269	2270	2271	2272	2273	2274	2275	2276	2277	2278	2279	2280	2281	2282	2283	2284	2285	2286	2287	2288	2289	2290	2291	2292	2293	2294	2295	2296	2297	2298	2299	2300	2301	2302	2303	2304	2305	2306	2307	2308	2309	2310	2311	2312	2313	2314	2315	2316	2317	2318	2319	2320	2321	2322	2323	2324	2325	2326	2327	2328	2329	2330	2331	2332	2333	2334	2335	2336	2337	2338	2339	2340	2341	2342	2343	2344	2345	2346	2347	2348	2349	2350	2351	2352	2353	2354	2355	2356	2357	2358	2359	2360	2361	2362	2363	2364	2365	2366	2367	2368	2369	2370	2371	2372	2373	2374	2375	2376	2377	2378	2379	2380	2381	2382	2383	2384	2385	2386	2387	2388	2389	2390	2391	2392	2393	2394	2395	2396	2397	2398	2399	2400	2401	2402	2403	2404	2405	2406	2407	2408	2409	2410	2411	2412	2413	2414	2415	2416	2417	2418	2419	2420	2421	2422	2423	2424	2425	2426	2427	2428	2429	2430	2431	2432	2433	2434	2435	2436	2437	2438	2439	2440	2441	2442	2443	2444	2445	2446	2447	2448	2449	2450	2451	2452	2453	2454	2455	2456	2457	2458	2459	2460	2461	2462	2463	2464	2465	2466	2467	2468	2469	2470	2471	2472	2473	2474	2475	2476	2477	2478	2479	2480	2481	2482	2483	2484	2485	2486	2487	2488	2489	2490	2491	2492	2493	2494	2495	2496	2497	2498	2499	2500	2501	2502	2503	2504	2505	2506	2507	2508	2509	2510	2511	2512	2513	2514	2515	2516	2517	2518	2519	2520	2521	2522	2523	2524	2525	2526	2527	2528	2529	2530	2531	2532	2533	2534	2535	2536	2537	2538	2539	2540	2541	2542	2543	2544	2545	2546	2547	2548	2549	2550	2551	2552	2553	2554	2555	2556	2557	2558	2559	2560	2561	2562	2563	2564	2565	2566	2567	2568	2569	2570	2571	2572	2573	2574	2575	2576	2577	2578	2579	2580	2581	2582	2583	2584	2585	2586	2587	2588	2589	2590	2591	2592	2593	2594	2595	2596	2597	2598	2599	2600	2601	2602	2603	2604	2605	2606	2607	2608	2609	2610	2611	2612	2613	2614	2615	2616	2617	2618	2619	2620	2621	2622	2623	2624	2625	2626	2627	2628	2629	2630	2631	2632	2633	2634	2635	2636	2637	2638	2639	2640	2641	2642	2643	2644	2645	2646	2647	2648	2649	2650	2651	2652	2653	2654	2655	2656	2657	2658	2659	2660	2661	2662	2663	2664	2665	2666	2667	2668	2669	2670	2671	2672	2673	2674	2675	2676	2677	2678	2679	2680	2681	2682	2683	2684	2685	2686	2687	2688	2689	2690	2691	2692	2693	2694	2695	2696	2697	2698	2699	2700	2701	2702	2703	2704	2705	2706	2707	2708	2709	2710	2711	2712	2713	2714	2715	2716	2717	2718	2719	2720	2721	2722	2723	2724	2725	2726	2727	2728	2729	2730	2731	2732	2733	2734	2735	2736	2737	2738	2739	2740	2741	2742	2743	2744	2745	2746	2747	2748	2749	2750	2751	2752	2753	2754	2755	2756	2757	2758	2759	2760	2761	2762	2763	2764	2765	2766	2767	2768	2769	2770	2771	2772	2773	2774	2775	2776	2777	2778	2779	2780	2781	2782	2783	2784	2785	2786	2787	2788	2789	2790	2791	2792	2793	2794	2795	2796	2797	2798	2799	2800	2801	2802	2803	2804	2805	2806	2807	2808	2809	2810	2811	2812	2813	2814	2815	2816	2817	2818	2819	2820	2821	2822	2823	2824	2825	2826	2827	2828	2829	2830	2831	2832	2833	2834	2835	2836	2837	2838	2839	2840	2841	2842	2843	2844	2845	2846	2847	2848	2849	2850	2851	2852	2853	2854	2855	2856	2857	2858	2859	2860	2861	2862	2863	2864	2865	2866	2867	2868	2869	2870	2871	2872	2873	2874	2875	2876	2877	2878	2879	2880	2881	2882	2883	2884	2885	2886	2887	2888	2889	2890	2891	2892	2893	2894	2895	2896	2897	2898	2899	2900	2901	2902	2903	2904	2905	2906	2907	2908	2909	2910	2911	2912	2913	2914	2915	2916	2917	2918	2919	2920	2921	2922	2923	2924	2925	2926	2927	2928	2929	2930	2931	2932	2933	2934	2935	2936	2937	2938	2939	2940	2941	2942	2943	2944	2945	2946	2947	2948	2949	2950	2951	2952	2953	2954	2955	2956	2957	2958	2959	2960	2961	2962	2963	2964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TABLE 1. SUMMARY OF DATA FOR THE 1960-1961 SEASON									
STATION	DATE	TIME	WIND DIRECTION	WIND SPEED (MPH)	WAVE HEIGHT (FT)	SEA STATE	WAVE PERIOD (SEC)	WAVE LENGTH (FT)	WAVE ENERGY (KCAL/M ²)
STATION 1	1960-12-15	08:00	090	12	1.5	1	8	100	0.1
	1960-12-15	12:00	090	15	2.0	2	7	120	0.2
	1960-12-15	16:00	090	18	2.5	3	6	140	0.3
	1960-12-15	20:00	090	20	3.0	4	5	160	0.4
STATION 2	1960-12-16	08:00	090	10	1.0	1	9	90	0.05
	1960-12-16	12:00	090	12	1.2	1	8	100	0.08
	1960-12-16	16:00	090	14	1.5	2	7	110	0.12
	1960-12-16	20:00	090	16	1.8	2	6	120	0.16
STATION 3	1960-12-17	08:00	090	8	0.8	1	10	80	0.03
	1960-12-17	12:00	090	10	1.0	1	9	90	0.05
	1960-12-17	16:00	090	12	1.2	2	8	100	0.08
	1960-12-17	20:00	090	14	1.5	2	7	110	0.12
STATION 4	1960-12-18	08:00	090	6	0.6	1	11	70	0.02
	1960-12-18	12:00	090	8	0.8	1	10	80	0.03
	1960-12-18	16:00	090	10	1.0	2	9	90	0.05
	1960-12-18	20:00	090	12	1.2	2	8	100	0.08
STATION 5	1960-12-19	08:00	090	4	0.4	1	12	60	0.01
	1960-12-19	12:00	090	6	0.6	1	11	70	0.02
	1960-12-19	16:00	090	8	0.8	2	10	80	0.03
	1960-12-19	20:00	090	10	1.0	2	9	90	0.05
STATION 6	1960-12-20	08:00	090	2	0.2	1	13	50	0.005
	1960-12-20	12:00	090	4	0.4	1	12	60	0.01
	1960-12-20	16:00	090	6	0.6	2	11	70	0.02
	1960-12-20	20:00	090	8	0.8	2	10	80	0.03
STATION 7	1960-12-21	08:00	090	1	0.1	1	14	40	0.002
	1960-12-21	12:00	090	3	0.3	1	13	50	0.005
	1960-12-21	16:00	090	5	0.5	2	12	60	0.01
	1960-12-21	20:00	090	7	0.7	2	11	70	0.02
STATION 8	1960-12-22	08:00	090	0.5	0.05	1	15	30	0.001
	1960-12-22	12:00	090	1	0.1	1	14	40	0.002
	1960-12-22	16:00	090	2	0.2	2	13	50	0.005
	1960-12-22	20:00	090	4	0.4	2	12	60	0.01
STATION 9	1960-12-23	08:00	090	0.2	0.02	1	16	20	0.0005
	1960-12-23	12:00	090	0.5	0.05	1	15	30	0.001
	1960-12-23	16:00	090	1	0.1	2	14	40	0.002
	1960-12-23	20:00	090	2	0.2	2	13	50	0.005
STATION 10	1960-12-24	08:00	090	0.1	0.01	1	17	10	0.0001
	1960-12-24	12:00	090	0.3	0.03	1	16	20	0.0005
	1960-12-24	16:00	090	0.5	0.05	2	15	30	0.001
	1960-12-24	20:00	090	1	0.1	2	14	40	0.002

NOTES: 1. WIND DIRECTION IS IN DEGREES TRUE. 2. WIND SPEED IS IN MILES PER HOUR. 3. WAVE HEIGHT IS IN FEET. 4. SEA STATE IS CLASSIFIED ACCORDING TO THE PILOT WAVE METHOD. 5. WAVE PERIOD IS IN SECONDS. 6. WAVE LENGTH IS IN FEET. 7. WAVE ENERGY IS IN KILOCALORIES PER SQUARE METER. 8. STATION 1 IS AT THE MOUTH OF THE RIVER. 9. STATION 2 IS AT THE MOUTH OF THE RIVER. 10. STATION 3 IS AT THE MOUTH OF THE RIVER. 11. STATION 4 IS AT THE MOUTH OF THE RIVER. 12. STATION 5 IS AT THE MOUTH OF THE RIVER. 13. STATION 6 IS AT THE MOUTH OF THE RIVER. 14. STATION 7 IS AT THE MOUTH OF THE RIVER. 15. STATION 8 IS AT THE MOUTH OF THE RIVER. 16. STATION 9 IS AT THE MOUTH OF THE RIVER. 17. STATION 10 IS AT THE MOUTH OF THE RIVER.

SELECTED CANADIAN LOAN CORPORATIONS (as at December 31st, 1960)

EXHIBIT G
Table 6

	Industry (9 Cos.)	Canada Permanent Mfge.	Credit Foncier Franco- Canadien	Eastern Can. Savings & Loan	Buron & Erie Mortgage	Lambton Loan & Investment	Ontario Loan & Debenture
Assets (\$ millions)							
Mortgages	470.68	181.08	81.67	41.06	117.45	9.51	36.04
Bonds	72.75	30.79	7.21	3.77	22.31	1.20	7.46
Stocks	25.70	9.96	7.30	.58	7.07	.33	.44
Total Assets	593.01	233.39	100.25	46.17	152.91	11.73	44.55
Liabilities (\$ millions)							
Deposits	135.40	64.51	—	6.58	52.32	3.27	8.67
Debentures	362.55	145.86	57.12	34.95	88.18	6.39	29.26
Total Liabilities to Public	513.78	214.82	66.57	42.56	141.05	9.78	38.22
Equity	79.23	18.77	33.68	3.60	11.85	1.95	6.33
Revenue (\$ millions)							
Mortgages	31.20	12.16	5.60	2.76	7.42	.61	2.47
Bonds	3.11	1.43	.01	.24	1.08	.02	.29
Stocks	1.47	.68	.34	.03	.38	.02	.03
Total Revenue	38.75	15.06	7.19	3.06	9.64	.69	2.30
Expenditures	29.55	12.08	4.58	2.44	7.85	.47	2.02
Net Earnings before Taxes	9.20	2.98	2.61	.62	1.79	.22	.88
Income Taxes	4.37	1.37	1.35	.30	.83	.10	.38
Net Profit	4.83	1.61	1.26	.32	.96	.12	.50
Dividends	3.83	1.60	1.06	.19	.57	.11	.30
Ratios							
Mortgages % Total Assets	79.37	77.59	81.47	88.93	76.81	81.07	80.90
Bonds % Total Assets	12.27	13.19	7.19	8.17	14.59	10.23	16.75
Stocks % Total Assets	4.33	4.28	7.28	1.41	6.02	3.47	.99
Deposits % Liabilities to Public	26.35	30.06	—	15.46	37.09	33.44	22.68
Debentures % Liab. to Public	70.57	67.96	85.80	82.12	62.52	65.34	76.56
Equity % Liab. to Public	15.42	8.75	50.59	8.46	8.40	19.94	16.56
Average rate earned on:							
- mortgages (1)	6.63	6.72	6.86	6.72	6.32	6.41	6.85
- bonds (1)	4.27	4.64	4.66	6.37	4.84	4.36	3.89
- stocks (1)	5.72	6.81	4.66	5.17	5.37	6.06	6.82
Revenue % Total Assets	6.53	6.45	7.17	6.63	6.30	5.88	6.51
Expenditures % Revenue	76.26	80.21	63.70	79.74	81.43	68.12	69.66
Net Profit % Total Assets	.81	.69	1.26	.69	.63	1.02	1.12
Net Profit % Equity	6.10	8.53	3.74	8.89	8.10	6.15	7.90
Dividends % Net Profit	79.30	99.38	84.13	59.38	59.38	91.67	60.00

(1) Calculated on 1960 revenues as a percentage of book value of mortgage and security investments outstanding as at December 31st, 1960, and is, therefore, not a weighted average return on investment.

SELECTED CANADIAN LOAN CORPORATIONS

E. & O. E.

EXHIBIT H

CREDIT UNIONS (1) (as at December 31)

Balance Sheet (\$ millions)	1960	1959	1958	1957	1956	1955	1954	1953	1952	1951
<u>Assets</u>										
- Loans (2)	425	397	320	258	226	174	151	129	94	76
- Mortgages (2)	387	341	295	262	236	211	171	155	131	113
- Investments	279	257	238	200	183	163	144	133	120	100
- Cash	166	129	127	108	94	87	71	51	56	51
- Other Assets	42	34	29	24	22	18	15	21	23	19
- Total Assets	1,299	1,158	1,009	852	761	653	552	489	424	359
<u>Liabilities</u>										
- Shares	474	402	341	272	232	194	161	133	102	81
- Deposits	721	658	594	515	468	409	350	320	294	253
- Other Liabilities	27	29	18	18	16	11	15	27	8	7
- Surplus Funds	77	69	56	47	45	39	26	9	20	18
- Total Liabilities	1,299	1,158	1,009	852	761	653	552	489	424	359
Number of Credit Unions	4,667	4,570	4,485	4,349	4,258	4,100	3,920	3,606	3,333	3,121
Number of Members (thousands)	2,544	2,360	2,187	2,060	1,870	1,731	1,561	1,434	1,260	1,138

(1) Includes Caisse Populaires and, Newfoundland Credit Unions from 1951-58.

(2) For 1951-55 the division of total loans between mortgage loans and other loans has been estimated.

Source: Bank of Canada Statistical Summary.

ATTACHED LISTING OF NAMES TO NAME, 2011-2012

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QUEBEC SAVINGS BANKS (as at December 31st)

Balance Sheet (\$ millions) Assets	1960	1959	1958	1957	1956	1955	1954	1953	1952	1951
Bank of Canada notes plus deposits with Bank of Canada and Chartered Banks.	25.6	26.4	24.7	26.3	20.3	18.5	19.5	14.7	13.6	16.7
Canadian Securities										
- Government of Canada	38.7	28.2	28.2	38.8	44.9	54.9	64.7	91.6	95.5	89.6
- Provincial	86.7	89.7	102.1	85.6	83.2	80.0	68.0	49.0	48.1	48.6
- Municipal	40.7	46.5	53.3	52.2	56.0	56.7	46.9	37.3	33.1	27.8
- Other	25.2	21.2	18.1	16.8	15.4	16.2	15.6	10.5	8.1	9.2
- Total	191.3	185.6	201.7	193.4	199.5	207.8	195.2	188.4	184.8	175.2
Mortgages and Loans										
- Insured N.H.A. Mortgages	10.4	10.7	10.7	10.1	9.2	5.6	2.7	-	-	-
- Other Mortgages	50.6	47.1	40.0	30.7	20.4	14.1	10.0	6.7	4.4	1.7
- Loans Otherwise Secured	8.0	7.1	6.5	8.8	7.8	5.9	5.0	4.6	4.4	4.3
- Unsecured loans	6.4	6.2	5.6	4.0	3.2	2.3	2.4	3.0	1.7	0.5
- Total	75.4	71.1	62.8	53.6	40.6	27.9	20.1	14.3	10.5	6.5
Other Assets	19.1	14.9	13.7	12.4	12.3	10.9	8.1	8.5	9.2	6.7
Total Assets	311.4	298.0	302.9	285.7	272.7	265.1	242.9	225.9	218.1	205.1
Liabilities										
Secured Advances from										
- Bank of Canada	-	-	-	-	-	-	-	-	-	-
- Chartered Banks	1.6	2.0	4.1	4.7	7.7	5.3	3.0	2.5	1.9	0.8
Deposits										
- Government of Canada	5.6	12.2	6.7	9.9	0.3	0.4	0.3	0.3	-	0.1
- Provincial Government	3.8	2.1	4.1	2.8	0.9	0.1	0.1	0.1	0.1	0.1
- Public	285.3	267.7	274.1	255.1	251.1	246.8	227.4	211.8	205.2	193.3
- Total	294.7	282.0	284.9	267.8	252.3	247.3	227.8	212.2	205.3	193.5
Other Liabilities	1.4	0.7	1.0	0.7	0.5	0.6	0.5	0.3	0.2	0.3
Shareholders Equity	13.7	13.3	12.9	12.5	12.2	11.9	11.6	10.9	10.7	10.5
Total	311.4	298.0	302.9	285.7	272.7	265.1	242.9	225.9	218.1	205.1

Source: Bank of Canada Statistical Summary.



APPENDIX I

RETAILING BONDS & STOCKS AND RISK CAPITAL

I N D E X

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Retailing Bonds & Stocks

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Variety of Securities A.517

2. Servicing the Retail Market A.518

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Supply of Information A.520

Training of Salesmen A.521

Protecting Investors' Capital A.522

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Public's Record & Attitude A.523

Raising Risk Capital A.525

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APPENDIX C

RETAILING BONDS & STOCKS AND RISK CAPITAL

TABLE I

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RETAILING BONDS & STOCKS

1. Description of the Retail Market

(1) The retail investor, for the purpose of this submission is taken as an individual who invests in securities. We believe that a better understanding of this market can be obtained if we describe retail investors in three categories. The actual limits established here should be understood in approximate terms only, as a general guide. We felt some actual figures would have to be stated in defining the categories, and they should therefore be used with the limitations they obviously possess.

I. The small investor -- an individual with up to approximately \$10,000 capital invested in securities.

II. The medium investor -- an individual with roughly \$10,000 to \$100,000 capital invested in securities.

III. The large investor -- the individual who has \$100,000 or more capital invested in securities.

(2) Until World War I, Canadian savings were small in volume and were invested chiefly in real estate and real estate mortgages or left on deposit with banks. The banks used most of their assets to make commercial loans, investing only a small portion in securities. Under circumstances such as these no capital market is likely to exist.

(3) Although the Canadian Bond business started in the 1880's when some of our member firms now engaged



This submission is taken as an individual who invests in securities. We believe there is a better understanding of this market can be obtained if we describe the actual market in three categories. The actual market established here should be understood in approximate terms only, as a general guide. We find some actual figures would have to be added in defining the categories and they should therefore be used with the limitations they obviously possess.

- I. The small investor -- an individual with up to approximately \$10,000 capital invested in securities.
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(3) Although in Canada -- and business seems



1 in the underwriting and distributing of securities were
2 founded, almost all Canadian financing was done in Great
3 Britain until 1914. English bond houses dominated the
4 market and Canadian dealers in most cases acted merely
5 as agents. After receiving the advice of a Canadian
6 dealer, the English bond firm would negotiate directly
7 with the borrower and underwrite the loan, assuming all
8 liability.

9 (4) Throughout this period the Canadian
10 dealers developed their retail business, confining their
11 activities largely to government and municipal bonds.
12 Methods of buying were rather elementary -- the Dealer
13 frequently combed local newspapers for notices of
14 municipalities and then contacted the local authorities
15 with a view to purchasing the entire issue for retail
16 sale. With the tremendous expansion in business which
17 came in 1900 - 1913 period, Canadian bond houses were
18 able to extend their operations to include a few issues
19 of companies engaged in public utility operation,
20 manufacturing and transportation.

21 (5) Bond sales had up to the First World War
22 (1914 - 1918) been confined to financial institutions
23 and to wealthy individuals. However, the great
24 increase in wealth in Canada prior to and during World
25 War I made possible the success of the first Victory
26 Loans which require a large number of small purchases.
27 Victory Loan campaigns were organized to make the
28 population "bond conscious" and to persuade the people
29 to loan their savings to the nation. These campaigns,
30 aided by the high interest rates, 5 per cent and 5½ per

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(4) Throughout this period the Canadian dealers developed their retail business, confining their activities largely to government and municipal bonds. Methods of buying were rather elementary -- the Dealer frequently combed local newspapers for notices of municipalities and then contacted the local authorities with a view to purchasing the entire issue for retail sale. With the tremendous expansion in business which came in 1900 - 1913 period, Canadian bond houses were able to expand their operations to include a few issues of companies engaged in public utility operation, manufacturing and transportation.

(5) Bond sales had up to the First World War (1914 - 1918) been confined to financial institutions and to wealthy individuals. However, the great increase in wealth in Canada prior to and during World War I made possible the success of the first Victory Loans which require a large number of small purchasers. Victory Loan campaigns were organized to make the population "bond conscious" and to persuade the people to loan their savings to the nation. These campaigns, aided by the high interest rates, 5 per cent and 7 1/2 per



cent, brought remarkable success.

(6) In 1915, 24,862 persons subscribed for \$78,729,000 of the first domestic War Loan issue. In 1918, over one million persons subscribed over \$660,000,000 to the Victory Loan of that year. The campaigns were organized at the Government's request, by the newly-formed "Bond Dealers' Association of Canada".

(7) During the period 1920-1930, almost \$6 billion was invested in capital goods, but, contrary to earlier periods of expansion, the amount of foreign capital which came in was much smaller. Less than \$1 billion of the \$6 billion came from the United States. The investment boom of the twenties was very largely financed out of Canadian savings. As a result Canadian financial houses benefitted greatly by the opportunities which presented themselves during this period.

(8) As in World War I, so in World War II, vast sums of money were raised internally by the Dominion Government through the organized sale of Victory Bonds. Almost the entire amount of Canada's war financing was carried out through domestic operations. In eleven war loan operations the Dominion Government borrowed some \$12,200 million from its citizens.

(9) A National War Finance Committee, almost wholly composed of investment dealers, was formed with headquarters in Ottawa and offices in each province. This committee acted as the coordinating body for the efforts of all financial firms in Canada and was the driving force behind the raising of funds for the Government through the sale of Victory Loan Bonds and



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Government through the sale of Victory Loan Bonds and



1 War Savings Certificates.

2 (10) The wide acceptance of Victory Bonds
3 stemmed from the committee's efforts in educating a large
4 selling force of qualified representatives. The concept
5 of a payroll savings plan was introduced to many employers
6 and its continued use today is evidence of its value.

7 (11) The Victory Loan campaigns of World War
8 II were responsible for hundreds of thousands of
9 Canadians owning, for the first time, an investment
10 security. Today, there are over two million individual
11 Canadians who own Government of Canada bonds. There is
12 no doubt that these securities, held by such a large
13 percentage of the citizens of the country, are a
14 stabilizing and a supporting factor in the period of
15 postwar readjustment through which we are still passing.
16 The habit of thrift which was encouraged during War Loan
17 years and which is renewed each year in the Canada
18 Savings Bond campaigns, has developed many new investors
19 and provides the basis on which a greater investment
20 business can be built in the years ahead.

21 The Understanding which the Retail
22 Investor has of Securities Markets

23 (12) THE SMALL INVESTOR will normally not have
24 a very good knowledge of securities markets. It has
25 been found that he will often have his money invested in
26 either of two extremes, i.e. exceedingly conservative,
27 where capital will be entirely in fixed income, high
28 grade bonds, or extremely speculative, with all funds
29 invested in penny gambling stocks. Of course, the
30 size of his holdings severely restricts the degree of



War Savings Certificates.

(10) The wide acceptance of Victory Bonds

stemmed from the committee's efforts in educating a large
selling force of qualified representatives. The concept
of a payroll savings plan was introduced to many employers
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1 diversification which is possible and in some cases
2 in recent years, the small investor has turned to mutual
3 funds, not necessarily of his own initiative. Very
4 rarely will the small investor be found who owns one or
5 two good investment grade stocks. The small investor
6 depends almost entirely upon his investment dealer,
7 stock broker or bank manager for guidance with his
8 investments, and the investment dealer actually goes out
9 and cultivates this business and does extensive work in
10 guiding and educating the small investor.

11 (13) THE MEDIUM INVESTOR quite often has a
12 growing account, being an advancing professional or
13 business man whose income is such that substantial
14 yearly savings are possible. Where this is the case,
15 he will often be relatively well informed, though too
16 busy to enter very fully into a study of investments, or
17 to follow the regular progress of his securities. He
18 too, will rely heavily upon his investment dealer or
19 stock broker and will follow his guidance in most
20 matters.

21 (14) The medium investor could also be someone
22 dependent upon this capital as a supplementary or even
23 sole source of income. This may be a retired, or semi-
24 retired person, a widow or dependent child who has
25 inherited the capital. Generally speaking, this
26 medium investor will not be too sophisticated or
27 knowledgeable in investment matters, and will tend to
28 follow the guidance of an investment dealer or stock
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30 individual dealers and the Investment Dealers' Association



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1 is aimed at this market.

2 (15) THE LARGE INVESTOR is quite different
3 from the small and medium investor. He will normally be
4 quite well informed on securities and markets, will
5 follow details of prices and know what is going on
6 from day to day. He will read financial journals and
7 periodicals, he may subscribe to one or more investment
8 counsel services and will likely do business with more
9 than one investment dealer or stock broker. This is a
10 more competitive market for the investment dealer, but
11 it is also one where the educational effort does not
12 need to be so great and where the costs of doing
13 business relative to the returns are less.

14 The Variety of Securities Sold
15 in the Retail Market

16 (16) The small investor is a market for bonds
17 of all types. In the Province of Quebec, and to some
18 extent in the Maritimes, the small investor is a good
19 market for municipal bonds, but this does not hold true
20 to the same extent in the other provinces. In practice,
21 in the past, the small investor has not constituted a
22 good source of capital for new sound enterprises, though
23 many have gone to outright speculation. There is no
24 reason why this should be so, but it does show that a
25 large job of education is still required, which, of
26 course, immensely increases the costs of doing business.

27 (17) The medium investor also is a good market
28 for all types of bonds, for good quality common stocks
29 and for serious new ventures. Quite often the medium
30 investor is in a high tax bracket, and is therefore
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1 secondary feature.

2 (18) The large investor provides a good
3 market for all types of securities from short term
4 Government of Canada bonds to common stock in a risk
5 venture.

6 2. Servicing the Retail Market

7 The Investment Dealers

8 (19) In another section of this brief, it is
9 shown that a large percentage of the investment dealers
10 in Canada are in the retail field.

11 (20) There are as well other financial
12 intermediaries in this field -- banks and stock brokers
13 sell securities to the retail market, and some mutual
14 funds have their own sales forces. The banks do not
15 send salesmen into the field as investment dealers do,
16 nor do stock brokers to any large extent. Almost
17 exclusively it is investment dealers who have salesmen
18 travelling and covering territories and carrying a broad
19 variety of securities.

20 Organization Required to
21 Service Retail Accounts

22 (21) In order to service retail accounts, the
23 investment dealer must first have the knowledge and
24 resources to select and buy the securities which are to
25 be offered to his clients. He then must have a system of
26 distribution -- a sales force with enough clients to
27 purchase the merchandise he has to offer.

28 (22) Developing a marketing organization is a
29 major task for an investment dealer. To competently
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1 salesmen qualified in the sense that they must be
2 familiar with investments, know how to assess securities
3 and, at the same time, be able to convey this to the
4 ordinary individual. This means the investment
5 dealer must have facilities to train salesmen, and have
6 sufficient resources to carry salesmen until they
7 become productive. In turn, the salesman must
8 develop a clientele, and cover a sufficient number of
9 investors so that a wide variety of securities can be
10 sold. He must have enough customers in each category.

11 (23) The investment dealers must also have
12 an analytical or research department to supply salesmen
13 with information and guidance. The size of this depart-
14 ment will depend on the size of the firm and the number
15 of salesmen in the field. Many refinements to research,
16 such as portfolio supervision, have been added in recent
17 years and the competition increasingly demands this type
18 of service.

19 (24) For investment dealers engaged in
20 underwriting, an underwriting department is required or
21 such work may be the chief function of the senior
22 personnel.

23 (25) An accounting department and a trading
24 department must be maintained, and the latter particular-
25 ly requires well trained personnel.

26 (26) The investment dealer must have a
27 communication system which puts his head office in touch
28 with out of town salesmen and branches. Larger dealers
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1 necessitates rapid communication.

2 (27) This organization will vary with size,
3 but in general it must be said the investment dealer
4 requires sufficient facilities to buy and sell
5 securities, to offer these to his customers, and to
6 provide those customers with sufficient information and
7 guidance on their investments.

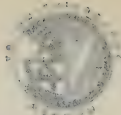
8 (28) It is quite apparent from the foregoing
9 section that the costs of doing retail business are high.

10 The Supply of Information

11 (29) A large percentage of the cost of the
12 Investment Dealers' Association goes to service the
13 retail investor, to educate him and to provide him with
14 instructive information. All dealers participate in
15 these association endeavours to educate the general
16 public in twoways. First, a substantial portion of the
17 regular fees go to educational work, and secondly,
18 investment dealers lend personnel who donate their time
19 freely to association endeavours.

20 (30) Investment dealers must, on an
21 independent basis, make available a broad variety of
22 informative material to the public. This could take the
23 form of a monthly letter discussing general conditions
24 or specific securities, it could be a weekly comment, or
25 a review of a company or a special write-up on a new
26 underwriting.

27 (31) To prepare this material, investment
28 dealers have research departments which may vary in size
29 from one man for a small or local dealer to possibly a
30 dozen people for a large national dealer. The information



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1 itself may vary from a brief comment for general
2 distribution to a 30 or 40 page study for select
3 distribution.

4 (32) Investment dealers are continually
5 attempting to interest new investors.

6 (33) Possibly the greatest number of new
7 investors come to an investment dealer from referrals by
8 his existing clientele. In addition, new investors
9 are attracted by advertising, in which some monthly or
10 other type of informative material might be offered.
11 When investors respond, they are followed up by the
12 firm's salesmen.

13 (34A) New investors can also be approached
14 directly when Government Bonds are being offered, and
15 this is widely done on Canada Savings Bond campaigns.
16 It should be pointed out that investment dealers go out
17 and aggressively sell Canada Savings Bonds to
18 established and new accounts. They do not just accept
19 unsolicited orders. This is considered to be a
20 valuable service since it puts Canada Savings Bonds into
21 the hands of many people who would not otherwise own
22 them, and provides a broader and a stronger distribution
23 of these securities.

24 (34B) It should be noted that investment
25 dealers are prohibited by law from directly approaching
26 new accounts at home for other than Government Bonds,
27 and this does have a restricting influence on the
28 development of new accounts.

29 The Training of Retail Salesmen

30 (35) Investment dealers have sales training



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1 programs. In most cases, this necessitates the
2 prospective salesman spending time in each of the
3 different operating departments so that he can become
4 thoroughly familiar with the total operation. During
5 this time, he attends sales meetings and is expected to
6 familiarize himself with investments and securities
7 markets. He is often required to complete one or both
8 of the two courses in the "principles and practices of
9 investment finance in Canada" offered by the Investment
10 Dealers' Association.

11 (36) Training is, of course, a continuous
12 process of education. The salesman should be able to
13 rely upon his firm for basic information and opinions
14 on conditions in general and securities in particular.
15 Protecting Investors' Capital

16 (37) Investment dealers continue to take an
17 interest in an enterprise after the securities of that
18 enterprise have been distributed by them to investors.
19 A representative will often sit on the Board of
20 Directors and even on the management committee and
21 financial statements and reports are obtained and
22 studied regularly. If a situation develops where
23 investors' capital may be in danger, investment dealers
24 will devote a considerable amount of time and, sometimes,
25 capital, to protect their clients' capital and to
26 attempt to restore the enterprise to a profitable
27 operation.

28 RISK CAPITAL

29 (38) It is quite apparent and an accepted
30 fact that risk capital is essential to the future



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Role of Capital

(38) It is quite apparent and is accepted
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development of this country.

Definition

(39) Risk capital, for the purposes of this submission, is taken to mean capital which is used for the development of new ventures, which ventures might be in primary or secondary industry. All types and variations of securities are used to raise risk capital in the retail markets. Bonds and debentures, convertible or with warrants attached, preferred stocks and common stocks are all employed, singly and in units.

Sources of Risk Capital

(40) The risk capital required in Canada has been and will continue to come from corporations, from institutions, from foreign investors and from small groups of large investors and from the general public. It is with this latter group that this submission is concerned.

The Public's Record and Attitude

(41) For purposes of this presentation, we should like to make a distinction between two different types of risk capital.

(a) That capital which is placed for long term investment in ventures, intelligently and seriously conceived and backed by reputable entrepreneurs. This is primarily the business of investment dealers.

(b) That capital which is invested for large, immediate profits, with little or no concern for the ultimate outcome



Department of Finance
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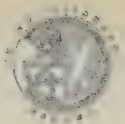
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1 of the enterprise. The degree of risk
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5 associated with mining and oil
6 development, and in some cases, it is
7 difficult to determine the integrity of
8 the scheme.

9 (42) It is our considered opinion that interest
10 has been developing in that type of capital described
11 under (a), but too many retail investors who do take
12 an interest in (a) will often exploit an early opportunity
13 for small short term capital gain and ignore the ultimate
14 benefits. Thus, the equity in many long term ventures
15 has shifted gradually from the public to institutional
16 and foreign investors, who are more sophisticated and
17 prepared to wait for long term development.

18 (43) The public will invest and hold the
19 equity of established and proven enterprises for long
20 periods of time, as witness the large retail interest
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23 regarded more as a speculation than a serious and
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1 it is our considered opinion that this is a long slow
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3 Raising Rick Capital

4 (44) This submission is concerned only with
5 risk capital raised by investment dealers.

6 (45) Ventures requiring capital may be
7 brought to an investment dealer by a promoter or
8 entrepreneur, who has either previously done business
9 with him, or who has been recommended by someone who
10 has. The investment dealer will study all the facts
11 and thoroughly examine the situation.

12 (46) Once the investment dealer is satisfied
13 that an enterprise is feasible, he will discuss and
14 suggest what form the financing should take. This
15 latter consideration is affected by many things,
16 including the current markets. Here, of course,
17 government policy is most important in setting the proper
18 environment, and this is true whether fixed income,
19 senior security financing or equity financing is
20 involved.

21 (47) After this has been done, the securities
22 must be sold. In the retailing operation, the
23 investment dealer will inform his salesman of the
24 details of the proposed issue of securities. How this
25 communication or information actually occurs will vary,
26 but normally the dealer will hold a sales meeting into
27 which he will bring all his salesmen. At this
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4 (48) Once he has a good understanding of
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6 his accounts to which the security is suitable. He
7 can then go to these accounts and sell this security.

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10 desire to make a sale, overlook the circumstances of
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12 are continually striving to overcome.

13 RETAILING BONDS AND STOCKS, AND RISK CAPITAL,
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15	<u>References</u>	(a) <u>Government of Canada Financing.</u> We
16		recommended that greater consideration
17		be given to the retail market when decid-
18	Pr. 11 Page A.515	ing terms of Government of Canada bond
19	Pr. 18 Page A.518	issues. Since 1959 - 1960 when various
20		5½ per cent Bonds were issued, few issues
21		of the Government of Canada have been
22		suitable for retail accounts. From
23		time to time bond issues tailored to
24		the retail market would be most approp-
25		riate. For instance, the retail holders
26		of medium term bonds should be given
27		the privilege of converting them into
28		longer term bonds. If this is not done,
29		the probability is that when the medium
30		term bonds become short term bonds, the



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Pr. 17
Page A.515
Pr. 18
Page A.517



1 retail holders will dispose of them
2 because of their low yield and will
3 no longer hold them when new issues of
4 long term securities are offered.

5 (b) Government Influence on Stability.

6 Government policies have an immense effect

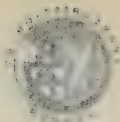
7 Pr. 46 on retail investors. Investment dealers
8 Page A.525

9 who sell and trade Government and
10 corporation securities and raise risk
11 capital must do so under stable market
12 conditions. Therefore, when disturbing
13 factors arise, Government leaders should
14 do everything possible to clarify the
15 situation and restore stability.

16 (c) Tax Credits. It is recommended that

17 Pr. 17 the percentage tax credit on dividends
18 Page A.517

19 which shareholders are now allowed be
20 raised for lower income groups; perhaps
21 the first \$500 of annual dividend income
22 would carry a higher percentage of tax
23 credits or even be tax free.
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retail holders will dispose of them
because of their low yield and will
no longer hold them when new issues of
long term securities are offered.

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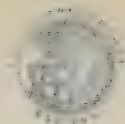
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Nethercut & Young
Toronto, Ontario

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TABLE 1

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STOCK BUSINESS

1. INTRODUCTION

In considering the operations of investment dealers, stock business obviously bulks very large and may indeed lay claim to pride of place. In the following pages, an effort is made to describe the nature of this business. It is first intended to examine briefly the various markets where Canadian securities are traded, and this will include a discussion of secondary distributions and the over-the-counter market. Most of the analysis will be concerned with the questions of the supply of and the demand for Canadian stocks. In this connection, some estimates will be made of net annual flows of funds from various sources into the Canadian stock market as well as of the existing importance of selected investors -- both individual and institutional -- in Canadian equity ownership. In addition, the part played by investment dealers and companies in helping to broaden stock ownership in Canada will be discussed briefly. The section will conclude with a number of recommendations.

2. THE STOCK EXCHANGES IN CANADA.

There are at present six exchanges in Canada. The relative size of their operations is indicated in the following table, which covers trading in 1960. As a basis of comparison, in the same year the number and value of shares traded on the New York Stock Exchange amounted to 987 million shares and \$38.0 billion respectively, and on the American Stock Exchange to 32 million shares and \$4.2 billion.



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TABLE I

Stock Exchange Transactions in 1960

	Industrial Shares (a)	Mines and Oils Shares	Total Shares	Clearing Values
	- - - -thousand shares - - - - (\$ thousands)			
Toronto	43,758	425,933	469,692	\$1,223,330
Montreal(b)	19,298	58,186	77,485	671,993
Vancouver	2,237	19,026	21,263	40,468
Calgary	196	9,812	10,009	2,760
Winnipeg	111	377	488	1,615

(a) Shares of industrials, public utilities, banks, etc.

(b) Montreal Stock Exchange and Canadian Stock Exchange combined.

Source: Toronto Stock Exchange

3. At the end of 1961 there were 1,117 stocks listed on the Toronto Stock Exchange with a quoted market value of \$61 billion, and 832 on the Montreal and Canadian Exchanges with a market value of \$59 billion. If account is taken of the substantial amount of duplication arising out of interlistings, the quoted market value of stocks on the Montreal and Toronto exchanges may be estimated at under \$62 billion, covering some 1,250 stocks. Of these, 21 with a market value of \$31 3/4 billion consisted of foreign firms, mainly a few large U.S. companies, whose stocks are listed in Canada as well as in the United States. Of the remainder, 168 with a market value of about \$1 billion were preferred stocks; this left listings having a value of \$29 billion made up of Canadian common, "A" and "B" stocks.

4. A number of Canadian shares are listed



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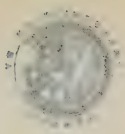


1 abroad, mainly in the United States. At the end of
2 1961, there were 11 Canadian companies listed on the
3 New York Stock Exchange and 94 on the American Stock
4 Exchange. Other centers where Canadian stocks are
5 traded include London, Brussels and Paris.

6 5. As a measure of trading activity,
7 Toronto clearing values in 1961 represented 4.1 per cent
8 of the total quoted market value of the list at the
9 end of the year. If the foreign stocks are excluded,
10 the proportion is raised to 8.6 per cent. A further
11 refinement is the removal of that section of the list
12 which is in effect untradeable; this includes stocks
13 that are owned on a permanent basis, notably inter-
14 company holdings. The Bank of Nova Scotia, in its
15 monthly review of October, 1960, estimates that 30 per
16 cent of Canadian securities fall into this class, which
17 would reduce the market value at the close of 1961 of
18 potentially active stocks on the Toronto list to \$20.5
19 billion and lift the measure of trading activity (clear-
20 ing values of that year as a proportion of the adjusted
21 total) to 12.3 per cent. It should be noted that 1961
22 was an active period in stock trading; in 1960, on the
23 other hand, which was slow, clearing values were only
24 half as large.

25 Secondary Distributions

26 6. In any discussion of the operations of
27 Canadian stock markets, the secondary method of
28 distribution must be mentioned. Usually, the offering
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1 exchanges. In Canada, the total value of the stock
2 offered in any one distribution might range between
3 \$250,000 to perhaps \$2 million or \$3 million. These
4 "secondaries", developed several years ago, have been
5 used more and more frequently in the past two or three
6 years as the most efficient method of distributing
7 stocks on a wide basis.

8 7. The vendor of the stock, by negotiation
9 with one dealer, will agree to terms of offering, such
10 as pricing and the commission to be paid to the
11 underwriting or distributing group. The originating
12 dealer usually invites other dealers to accept an under-
13 writing position in the group. This group accepts firm
14 stock at the offering prices, less a commission
15 previously arranged.

16 8. The price at which the offering will be
17 made usually bears a very close relationship to the
18 quoted market on the Stock Exchange for the stock.
19 Generally speaking, the offering price is on the bid
20 side of the market or, in some cases, slightly below
21 the bid side. Various factors must be considered when
22 pricing the offering, such as general market conditions,
23 outlook for the company whose stock is being offered,
24 and the popularity of the stock being offered.

25 9. The commission paid on the offering, as
26 it has developed in the Canadian market, usually amounts
27 to double the minimum Stock Exchange commission on a
28 stock selling at the offering price and, in some cases,
29 there may be an additional small commission which might
30 be considered a finder's fee. It might be noted that



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1 commissions paid on secondary distributions in the U.S.
2 market range from about four to six and a half times the
3 average minimum commission rate.

4 Stock Exchange Commissions in Canada

5 10. Since the late 1930's there have been
6 two revisions of the scale of commissions charged by
7 brokers for effecting transactions for their clients.
8 The first realignment in 1945 involved almost entirely
9 an upward revision of charges in all classes. The
10 second was a combination of upward revisions and
11 reclassifications which removed certain anomalies in
12 the fees charged to clients. In themselves, the upward
13 adjustments were not substantial in relation to the
14 volume of money involved in many transactions. It
15 should be noted that, in the post-war period, demands
16 for added services, communications and servicing of
17 transactions have required a considerable increase in
18 operating expenditures by brokers. A further revision of
19 these brokerage charges may have to be made so as to
20 reflect more fully the dollar value of the transaction
21 and the true cost of effecting the smaller transactions.
22 In other words, commissions may have to be re-examined
23 in the light of operating expenditures on services,
24 the maintenance of which is necessary if the full
25 interests of clients are to be served. This would be
26 done only after a thorough and exhaustive review of the
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1 The Over-the-Counter Market

2 11. The Canadian over-the-counter market
3 covers virtually all transactions of the following
4 securities: Government, Provincial and Municipal
5 bonds and corporate debentures; in addition, many stock
6 issues, which for one reason or another are not listed
7 on an exchange, are traded on the market, as well as
8 most mutual fund shares. Among the quality stocks
9 involved, mention may be made of those of a number of
10 insurance companies and trust companies. Transactions
11 also take place in several European securities,
12 particularly of British origin. The over-the-counter
13 market is extensively used by investment dealers,
14 providing an initial market for new issue securities.
15 Most new industrial issues, being offered for the first
16 time to the Canadian public, initially trade over the
17 counter prior to becoming listed on recognized Canadian
18 stock exchanges. Rights offerings to shareholders in
19 a good many cases trade over the counter during a
20 limited period until the right expires.

21 12. In the natural resource field, the over-
22 the-counter market facilitates trading in a wide variety
23 of low-priced speculative securities. These stocks
24 usually represent small exploration attempts to develop
25 natural resources in Canada. Usually, where success is
26 achieved in the development of a natural resource, the
27 stock in question will qualify for listing on one of
28 the stock exchanges in the country; the vast majority
29 of these speculative vehicles, however, remains
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1 circumstances within their area of activity.

2 13. The over-the-counter market is vast and
3 complex and not located in any given meeting place.
4 From coast to coast, traders in investment and
5 brokerage firms are constantly in touch with each other
6 through private telegraph wires, telephones and other
7 communication facilities at their disposal. In the
8 over-the-counter market, the dealer acts either as
9 principal or as agent. Acting as principal, he buys or
10 sells securities net without any commission charge; in
11 acting as an agent he usually adheres to commissions
12 prescribed by the Montreal and Toronto Stock Exchanges.
13 Very often, the over-the-counter dealer is obliged to
14 take inventory positions in securities which he may be
15 trading. He therefore risks his own capital in the
16 maintenance of various positions in anticipation of a
17 future demand for the security in question.

18 14. Because so many securities of varying
19 characteristics are traded over the counter by large,
20 medium-sized and small investment firms, it is impossible
21 to determine the gross dollar turn-over for any given
22 period of time. At certain times, particularly during
23 the creation of brand new industries, such as uranium,
24 oil and gas and the related pipelines, activity in the
25 over-the-counter markets increases sharply; the same
26 is true during periods of traditional natural resource
27 development. At other times, trading in over-the-counter
28 securities shrinks, reflecting movements only in a
29 limited number of Canadian securities. As compared
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1 in stocks is extremely small. In the United States,
2 there are about 5,000 unlisted issues quoted daily in
3 American papers as opposed to only 1,600 stocks listed
4 on the New York Stock Exchange. In Canada, the reverse
5 would be the case, excluding penny mining shares, in
6 that there are far more shares of Canadian companies
7 listed on recognized stock exchanges than there are
8 traded in the Canadian over-the-counter market.

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10 15. THE SUPPLY OF STOCKS

11 The discussion now turns on the supply of
12 shares, which constitutes one of the most important
13 topics falling within the broad subject of stock
14 business. While frequent mention is made of this
15 supply, it is hard to analyze in terms of actual
16 quantities. At any given moment in time, the supply
17 may be expressed as the value of stocks on the Canadian
18 exchanges, adjustments having been made for those
19 listed on more than one exchange, for foreign stocks
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21 proportion which is so unlikely to be traded that it
22 cannot be regarded as forming part of any potential
23 offering. A second measure of supply is the total of
24 new stocks, net of redemptions, issued over a period of
25 years. In Table II, this information is given for the
26 period since 1952.

27 16. The significance of these figures is
28 discussed in detail in the section relating to
29 Corporation Finance. Suffice it to say here that: (a)
30 there has been a steady post-war rise in the proportion



there are about 2,000 unlisted issues quoted daily in American papers as opposed to only 1,600 stocks listed on the New York Stock Exchange. In Canada, the reverse would be the case, excluding penny mining shares, in that there are far more shares of Canadian companies listed on recognized stock exchanges than there are traded in the Canadian over-the-counter market.

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TABLE II

Net New Security Issues

	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961 *</u>	Total 1952-1961	%
						million	dollars.					
Common Stocks	\$ 223	185	147	367	514	426	287	331	182	242	\$ 2,904	36
Preferred Stocks	<u>16</u>	<u>51</u>	<u>25</u>	<u>95</u>	<u>175</u>	<u>89</u>	<u>25</u>	<u>73</u>	<u>52</u>	<u>44</u>	<u>645</u>	8
Total Equity	239	236	172	462	689	515	312	404	234	286	3,549	44
Corporate Bonds	<u>373</u>	<u>375</u>	<u>445</u>	<u>324</u>	<u>794</u>	<u>954</u>	<u>654</u>	<u>108</u>	<u>290</u>	<u>275</u>	<u>4,592</u>	56
Total Financing	\$ 612	611	617	786	1,483	1,469	966	512	524	561	\$ 8,141	100%

* Does not include the retirement of \$111 million of B.C. Electric Co. held by the parent company, but does include partial distribution of \$86 million to shareholders of B.C. Power.

Source: Bank of Canada Statistical Summary, December, 1961; Financial Supplement, 1958.

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1901

Enrico De Luca, 1893



1 of business capital expenditures financed internally;
2 (b) in the period since 1952, the dollar amount of
3 business external financing rose to a peak in 1956-
4 1957 and has since subsided to less than half its
5 record levels; (c) within this total, somewhat more than
6 two-fifths has been accounted for by equity financing.

7 17. Among the many factors affecting the
8 supply of Canadian stocks, the following are among the
9 more important:

10 (a) Perhaps the most obvious, is the nature
11 of Canada's economic development. The emphasis on
12 the exploitation of Canada's natural resources is most
13 strikingly reflected on the board of the Toronto Stock
14 Exchange where "penny" mining shares abound; close to
15 half of the stocks listed are in fact priced at less
16 than \$5.00. The absence of "space" stocks, the limited
17 number of electronics, chemical and drug stocks, etc.,
18 again reflect the character of industrial growth in this
19 country.

20 (b) The great importance of foreign ownership
21 in a number of Canadian industries has resulted either
22 in the presence in Canada of wholly-owned subsidiaries in
23 the operations of which the public cannot acquire a
24 direct interest, or in the effective withdrawal from
25 the market of the majority of a company's stock; Ford
26 Motor Company of Canada, 75 per cent owned by Ford of
27 U.S., is an example of the latter process. The subject
28 is discussed at greater length in a separate section.

29 (c) The extent of public ownership is a third
30 general determinant of the availability of Canadian



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(p) in the period since 1952, the dollar amount of

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the market of the majority of a company's stock; Ford

Motor Company of Canada, 75 per cent owned by Ford of

U.S., is an example of the latter process. The subject

is discussed at greater length in a separate section.

(c) The extent of public ownership is a third

general determinant of the availability of Canadian



1 equities; its effects are most obvious in transportation
2 and utilities; the expropriation of B.C. Electric is the
3 most recent case in point.

4 (d) The mutualization of insurance companies
5 provides another example of the withdrawal of stocks
6 from the market. In the three years 1958-1960, such
7 purchases averaged \$52 million annually.

8 (e) Among considerations internal to
9 corporations that affect the supply, mention should be
10 made of the incentive to debt financing provided by the
11 fact that interest costs are pre-taxed; indeed, every
12 time the corporate tax rate is increased, this incentive
13 strengthens.

14 (f) Also militating against equity financing
15 is the prospect of further inflation; clearly the
16 possibility of borrowing money having a certain
17 purchasing power and eventually repaying it in currency
18 with a reduced purchasing power acts as a stimulus to
19 debt financing.

20 18. There are, at the same time, a number of
21 expansionary influences on the supply of stocks. The
22 absence of a capital gains tax, by enabling profits to
23 be realized with no penalty to the stockholder, provides
24 a real stimulus to trading. The 1954 revision of the
25 Bank Act, which permitted the chartered banks to exclude
26 certain classes of their shareholders from share
27 offerings, enabled them to escape the disclosure require-
28 ments of the U.S. Securities Exchange Commission, and has
29 greatly stimulated the issue of bank shares through
30 rights offerings. As a general comment, because of the

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most recent case in point.

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1 existence of S.E.C. regulations, rights issues of
2 Canadian companies are sometimes not offered to U.S.
3 residents, and this has the result of adding to the
4 supply of stocks on the Canadian markets. Perhaps,
5 though, the most important reasons for the steadiness
6 of the flow of new equity issues in the post-war period
7 are: a) some companies do not have the financial
8 standing and/or lack the type of assets that would permit
9 financing at a reasonable cost through the sale of long
10 term debt; b) other companies that do not suffer from
11 these limitations nevertheless make stock issues because
12 of the need to build up their equity base; understandably,
13 this is particularly true where retained earnings are
14 relatively unimportant and is characteristic of certain
15 kinds of utilities, as for instance pipe lines and Bell
16 Telephone.

17 19. From these few comments, it is apparent
18 that among the forces affecting the supply of Canadian
19 equities, a significant number have a restrictive
20 influence.

21 20. STOCK OWNERSHIP AND SOURCES OF DEMAND FOR STOCKS

22 The incidence of stock holdings among
23 individual Canadians and the importance of financial
24 institutions in Canada in the ownership of stocks are
25 subjects which are of immense interest but on which, as
26 a general rule, only limited statistical information
27 is available.

28 Individual Investors

29 21. Looking first of all at the position of
30 individuals, some broad comments can be made on the



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19. From these few comments, it is apparent that among the forces affecting the supply of Canadian equities, a significant number have a restrictive influence.

20. STOCK OWNERSHIP AND CONTROL IN CANADA

The incidence of stock holdings among individual Canadians and the importance of financial institutions is shown in the statistics of public companies which are of interest to us in this connection. A general conclusion which may be drawn from the available data is available.

Individual Investors

21. Looking first of all at the position of individuals, some broad comments can be made on the



TABLE III

Percentage of Non-Farm Families and Unattached
Individuals Owning Stocks within Selected Income Groups

	Income Groups		All Families and Unattached Individuals
	Under \$2,000	\$2,000- \$4,999	
1959 Spring	3.1%	5.1%	9.2%
1956 March	4.0	5.1	8.9

Note: The total of families and unattached individuals was 4,460,000 in 1958 and 4,051,000 in 1955; the family is defined as a group of individuals sharing a common dwelling unit and related by blood, marriage or adoption. Unattached individuals are persons living by themselves or rooming in a household where they are not related to other household members.

Source: D.B.S. Incomes, Liquid Assets and Indebtedness of Non-Farm Families in Canada 1955, 1958.



III. EIGHT

Percentage of Non-Farm Families and Unattached

Year	Total	Income Groups		Total	Percentage	Unattached
		\$5,000-\$9,999	\$10,000 and over			
1929	3.4	1.2	2.2	1.8	2.0	2.0
1930	3.4	1.2	2.2	1.8	2.0	2.0
1931	3.4	1.2	2.2	1.8	2.0	2.0
1932	3.4	1.2	2.2	1.8	2.0	2.0
1933	3.4	1.2	2.2	1.8	2.0	2.0
1934	3.4	1.2	2.2	1.8	2.0	2.0
1935	3.4	1.2	2.2	1.8	2.0	2.0
1936	3.4	1.2	2.2	1.8	2.0	2.0
1937	3.4	1.2	2.2	1.8	2.0	2.0
1938	3.4	1.2	2.2	1.8	2.0	2.0
1939	3.4	1.2	2.2	1.8	2.0	2.0
1940	3.4	1.2	2.2	1.8	2.0	2.0
1941	3.4	1.2	2.2	1.8	2.0	2.0
1942	3.4	1.2	2.2	1.8	2.0	2.0
1943	3.4	1.2	2.2	1.8	2.0	2.0
1944	3.4	1.2	2.2	1.8	2.0	2.0
1945	3.4	1.2	2.2	1.8	2.0	2.0
1946	3.4	1.2	2.2	1.8	2.0	2.0
1947	3.4	1.2	2.2	1.8	2.0	2.0
1948	3.4	1.2	2.2	1.8	2.0	2.0
1949	3.4	1.2	2.2	1.8	2.0	2.0
1950	3.4	1.2	2.2	1.8	2.0	2.0
1951	3.4	1.2	2.2	1.8	2.0	2.0
1952	3.4	1.2	2.2	1.8	2.0	2.0
1953	3.4	1.2	2.2	1.8	2.0	2.0
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1960	3.4	1.2	2.2	1.8	2.0	2.0
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1962	3.4	1.2	2.2	1.8	2.0	2.0
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1964	3.4	1.2	2.2	1.8	2.0	2.0
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1966	3.4	1.2	2.2	1.8	2.0	2.0
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1968	3.4	1.2	2.2	1.8	2.0	2.0
1969	3.4	1.2	2.2	1.8	2.0	2.0
1970	3.4	1.2	2.2	1.8	2.0	2.0
1971	3.4	1.2	2.2	1.8	2.0	2.0
1972	3.4	1.2	2.2	1.8	2.0	2.0
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1980	3.4	1.2	2.2	1.8	2.0	2.0
1981	3.4	1.2	2.2	1.8	2.0	2.0
1982	3.4	1.2	2.2	1.8	2.0	2.0
1983	3.4	1.2	2.2	1.8	2.0	2.0
1984	3.4	1.2	2.2	1.8	2.0	2.0
1985	3.4	1.2	2.2	1.8	2.0	2.0
1986	3.4	1.2	2.2	1.8	2.0	2.0
1987	3.4	1.2	2.2	1.8	2.0	2.0
1988	3.4	1.2	2.2	1.8	2.0	2.0
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1993	3.4	1.2	2.2	1.8	2.0	2.0
1994	3.4	1.2	2.2	1.8	2.0	2.0
1995	3.4	1.2	2.2	1.8	2.0	2.0
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2000	3.4	1.2	2.2	1.8	2.0	2.0
2001	3.4	1.2	2.2	1.8	2.0	2.0
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2003	3.4	1.2	2.2	1.8	2.0	2.0
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2006	3.4	1.2	2.2	1.8	2.0	2.0
2007	3.4	1.2	2.2	1.8	2.0	2.0
2008	3.4	1.2	2.2	1.8	2.0	2.0
2009	3.4	1.2	2.2	1.8	2.0	2.0
2010	3.4	1.2	2.2	1.8	2.0	2.0
2011	3.4	1.2	2.2	1.8	2.0	2.0
2012	3.4	1.2	2.2	1.8	2.0	2.0
2013	3.4	1.2	2.2	1.8	2.0	2.0
2014	3.4	1.2	2.2	1.8	2.0	2.0
2015	3.4	1.2	2.2	1.8	2.0	2.0
2016	3.4	1.2	2.2	1.8	2.0	2.0
2017	3.4	1.2	2.2	1.8	2.0	2.0
2018	3.4	1.2	2.2	1.8	2.0	2.0
2019	3.4	1.2	2.2	1.8	2.0	2.0
2020	3.4	1.2	2.2	1.8	2.0	2.0
2021	3.4	1.2	2.2	1.8	2.0	2.0
2022	3.4	1.2	2.2	1.8	2.0	2.0
2023	3.4	1.2	2.2	1.8	2.0	2.0
2024	3.4	1.2	2.2	1.8	2.0	2.0
2025	3.4	1.2	2.2	1.8	2.0	2.0
2026	3.4	1.2	2.2	1.8	2.0	2.0
2027	3.4	1.2	2.2	1.8	2.0	2.0
2028	3.4	1.2	2.2	1.8	2.0	2.0
2029	3.4	1.2	2.2	1.8	2.0	2.0
2030	3.4	1.2	2.2	1.8	2.0	2.0

Source: D.B.2. Families in Canada 1922, 1923, 1924, 1925, 1926, 1927, 1928, 1929, 1930, 1931, 1932, 1933, 1934, 1935, 1936, 1937, 1938, 1939, 1940, 1941, 1942, 1943, 1944, 1945, 1946, 1947, 1948, 1949, 1950, 1951, 1952, 1953, 1954, 1955, 1956, 1957, 1958, 1959, 1960, 1961, 1962, 1963, 1964, 1965, 1966, 1967, 1968, 1969, 1970, 1971, 1972, 1973, 1974, 1975, 1976, 1977, 1978, 1979, 1980, 1981, 1982, 1983, 1984, 1985, 1986, 1987, 1988, 1989, 1990, 1991, 1992, 1993, 1994, 1995, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014, 2015, 2016, 2017, 2018, 2019, 2020, 2021, 2022, 2023, 2024, 2025, 2026, 2027, 2028, 2029, 2030.



1 incidence of equity ownership among various income
2 groups. In Table III the findings of two surveys
3 covering non-farm families and unattached individuals
4 in Canada are presented. It deserves to be pointed out
5 that, under the wording of the questionnaire, both
6 publicly traded common and preferred stocks and those
7 traded over the counter were included; the survey was
8 not limited to Canadian equities; with respect to the
9 treatment given to mutual funds, while the wording was
10 somewhat ambiguous, it may be assumed that most mutual
11 fund shareholders will have regarded themselves as
12 stockholders in their replies.

13 22. From Table III, it appears that in the
14 spring of 1959 a little over 9 per cent of Canadian
15 families and unattached individuals owned stocks, an
16 increase of 50,000 from three years previously. Within
17 the various income groups, it is not surprising to
18 find by far the greatest incidence of ownership among
19 the higher brackets. It should be emphasized that these
20 figures must be treated with caution (particularly those
21 for 1956 which are based on a considerably smaller
22 sample than was the case in 1959); nevertheless, it is
23 of some interest to note that the overall percentages
24 are not very different from those obtained in the United
25 States: a U.S. survey (Federal Reserve Bulletin, June,
26 1955) revealed that 8 per cent of U.S. family units
27 were stockholders.

28 23. In Table IV, some idea can be obtained
29 of the concentration of stock ownership. In
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1 out that they refer only to taxable persons, that is to
2 say to persons whose taxable income exceeded their
3 exemptions; (that this should not be too serious a
4 limitation, however, is suggested by the fact that in
5 1959 dividend income reported in non-taxable returns
6 amounted to only \$10,383,000, as against a total of
7 \$296,218,000 in taxable returns). As in Table III, the
8 findings relate to both preferred and common stocks;
9 unlike the earlier table, however, the information is
10 limited to holdings of stocks of taxable Canadian
11 corporations, since it is only on these that the credit
12 may be claimed. As to the reliability of these taxation
13 figures, the incentive to accurate reporting provided
14 by the dividend tax credit is obviously important; it
15 has been estimated that the amount of dividends reported
16 on the individual income tax returns represents more
17 than 90 per cent of actual dividend receipts.

18 24. Not surprisingly, the incidence of stock
19 ownership indicated in Table IV (those claiming a
20 dividend tax credit as a percent of total taxable
21 persons) is lower throughout the various income groups
22 than in Table III, where no distinction is drawn
23 between holdings of dividend-paying and non-dividend
24 paying stocks. Perhaps the most interesting feature
25 of the table is the evidence it provides of the
26 concentration of stock ownership; 55,000 individuals,
27 representing little more than $1\frac{1}{4}$ per cent of all
28 taxable persons in Canada, accounted for over 60 per
29 cent of dividend income reported in all taxable returns.

30 25. There are no figures on the actual market



25. There are no figures on the actual number of dividend income reported in all taxable returns. Taxable persons in Canada, accounted for over 60 per cent of dividend income reported in all taxable returns. representing little more than 1 1/2 per cent of all concentration of stock ownership; 52,000 individuals of the table is the evidence it provides of the paying stocks. Perhaps the most interesting feature between holdings of dividend-paying and non-dividend then in Table III, where no distinction is drawn persons) is lower throughout the various income groups dividend tax credit as a percent of total taxable ownership indicated in Table IV (those claiming a 24. Not surprisingly, the incidence of stock than 90 per cent of actual dividend receipts. on the individual income tax returns represents more has been estimated that the amount of dividends reported by the dividend tax credit is obviously important; it figures, the incentive to accurate reporting provided may be claimed. As to the reliability of these taxation corporations, since it is only on these that the credit limited to holdings of stocks of taxable Canadian unlike the earlier table, however, the information is findings relate to both preferred and common stocks; \$296,218,000 in taxable returns). As in Table III, the 1959 dividend income reported in non-taxable returns amounted to only \$10,383,000, as against a total of 1959 dividend income reported in non-taxable returns exemption; (that this should not be too serious a limitation, however, is suggested by the fact that in



TABLE IV

Dividend Income in 1959

Number of Taxable Persons	Under \$2,000	\$2,000- \$4,999	\$5,000 \$6,999	\$7,000 \$9,000	\$10,000 and over	All Income Groups
	662,240	2,655,522	593,143	204,128	127,457	4,242,490
No claiming Dividend Tax credit	15,725	105,397	50,115	37,344	55,022	263,603
As % of No. of Taxable persons	2.4%	4.0%	8.4%	18.3%	43.2%	6.2%
Total Dividends Received (\$000)	\$ 7,044	\$ 49,140	\$27,548	\$ 31,998	\$180,488	\$296,218
As % of Total for all Income Groups	2.4%	16.6%	9.3%	10.8%	60.9%	100%

Source: Department of National Revenue



1 value of individuals' stock holdings. Statistics on
2 the net flows of personal savings into the stock market
3 are also conspicuously absent; it is nonetheless true
4 that Canadians enjoy a number of incentives to stock
5 ownership, which residents of other countries, notably
6 the United States, lack. The absence of a capital
7 gains tax, mentioned in the section dealing with the
8 supply of stocks, removes a deterrent to equity ownership
9 which exists in countries where this tax is present.
10 The elimination in the budget of December, 1960, of the
11 4 per cent surtax paid by persons with investment income
12 of \$2,500 or more -- so long as the income is from
13 Canadian sources -- provided an incentive to Canadian
14 stock ownership. Finally, this form of tax encouragement
15 exists in what is perhaps its most effective form in
16 the 20 per cent dividend tax credit which is allowed
17 Canadian residents on dividend income from Canadian
18 corporations; incentives of a somewhat similar nature --
19 but less powerful -- exist also in the depletion
20 allowances granted on dividends of oil, gas or mining
21 companies.

22 Institutional Investors

23 26. The distinction that is commonly drawn
24 between individual investors and institutional investors
25 is, it must be admitted, somewhat forced. Considering
26 the question of the incidence of share ownership, for
27 instance, there is a danger of double counting; an
28 individual owning shares in a mutual fund or having
29 funds administered by a trust company, a proportion of
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1 stockholder and will have been covered in the
2 questionnaire discussed in the preceding section. The
3 fact remains, however, that financial intermediaries, by
4 their very nature, constitute major repositories of
5 funds, which sometimes lend themselves to analysis; it
6 is important to be aware of the different investment
7 policies of these intermediaries and of the changes
8 that may be taking place in such policies; indeed, one
9 of the most interesting post-war developments has been
10 the growth in the so-called contractual forms of personal
11 saving, which is best illustrated in the rapid expansion
12 of life insurance companies and pension funds.

13 27. The information available on institutions
14 varies widely from being extensive in the case of pension
15 funds to largely non-existent in that of administered
16 trust company funds. For the purposes of this
17 submission, there are two questions to which it seems
18 important to try to find answers: (a) what is the
19 net annual flow of fresh money into Canadian common
20 stocks from the various institutions, and (b) what is the
21 importance of existing holdings in relation to the
22 Canadian market. To answer the first question, it would
23 be necessary to have book value figures of Canadian
24 common stock holdings over a period of years, the
25 difference from year to year indicating the net
26 participation in the Canadian equity market of each
27 type of institution. For a second question, the market
28 values of such investments are needed. In the following
29 discussion, it will become apparent that in many cases
30 both sets of figures are not available and in some cases,



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TABLE V
Changes in Stock Holdings (Book Value)

	1955	1956	1957	1958	1959	1960	1955-1959
New Stock Issues	462	689	515	312	404	234	2,382
Changes in stock holdings of -							
Life Insurance Companies	14	8	1	21	11	5	55
Fire & Casualty Companies	9	8	5	8	7	N.A.	37
Trust Companies	1	6	3	1	4	2	15
Mortgage Loan Companies	7	5	1	9	3	3	25
Pension Funds	N.A.	N.A.	21	43	53	55	117
Investment Companies	44	51	35	24	77	47	231
NRO Funds	68	70	74	14	-10	-30	216
Other foreign portfolio investments	140	183	99	101	150	96	673
Total	283	331	239	221	295	-	1,369
As % of New Stock Issues	61.2%	48.0%	46.4%	71.2%	73.0%	-	57.5%

Sources: Bank of Nova Scotia Monthly Review, October 1960;
Investment company reports; some figures are partially estimated.



1 that are published, are subject to serious
2 limitations.

3 28. In Table V changes in the book value
4 holdings of selected institutions as well as in foreign
5 portfolio investments are related to net new stock
6 issues. Some of these findings are examined in greater
7 detail in the following pages. As a general comment,
8 the figures should be used with extreme caution.

9 29. Life Insurance Companies

10 In Table VI, a breakdown of the assets of
11 life insurance companies at book values is presented.

12 30. One of the most striking features of
13 this table is the small proportion of assets invested in
14 common stocks; indeed, in the post-war period, life
15 insurance company holdings as a proportion of total
16 assets have never approached the 15 per cent statutory
17 limit established in 1932.

18 31. One difficulty in using book values to
19 determine the net flows of investment funds into
20 Canadian common stocks is the practice of insurance
21 companies of writing down such figures; the incentive
22 is provided by the fact that they are under statutory
23 obligation to value their assets as of some particular
24 period and show a state of complete solvency. It is
25 therefore not necessarily true, for instance, that in
26 1960 the net inflow for equity investment was \$5 million
27 (\$176 million less \$171 million). In this connection,
28 the monthly statistics covering the investment
29 transactions of the 12 major life companies, published by
30 the Bank of Canada, are of limited help, since they



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Investment

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the Bank of Canada, are of limited help, since they



TABLE VI

Life Insurance Company Assets

As at December 31,	1954	1959	1960
	\$ million %	\$ million %	\$ million %
Canadian Securities	3,045	3,740	3,980
	58.2	50.0	49.7
Bonds	2,929	3,510	3,755
Preferred & common	116	171	176
Own Stock remutualization	-	59	49
	-	0.7	0.6
Foreign Securities	169	186	191
	3.2	2.5	2.4
Bonds	111	116	121
Preferred & common	58	70	70
	1.1	0.9	1.5
Mortgages	1,519	2,787	3,011
	29.1	37.3	37.6
Other	493	761	825
	9.5	10.2	10.3
Total Assets:	5,226	7,474	8,007
	100%	100%	100%

NOTE: Life branch assets of all companies registered under the Federal Insurance Acts, comprising all assets physically held in Canada by Canadian companies and British and foreign companies; Canadian dollar assets held outside Canada are excluded.

Source: Bank of Canada Statistical Summary, August 1961

on the other hand are excluded.

companies and foreign companies; companies dollar assets held
 assets, companies all assets dollar assets held in assets of companies
 income: The French assets of all companies registered under the Federal Insurance

Total Assets:

Other

Assets

Preferred & common
 Bonds

Preferred Securities

and Stock Investments
 Preferred & common

Assets

As at December 31,

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3,000

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IV Assets

Assets

Assets

Assets

Assets

Assets

Assets



1 include purchases of insurance stocks for mutualization
2 purposes. It is possible, however, to develop from the
3 Reports of the Superintendent of Insurance general
4 estimates; this source has the added virtue that
5 Canadian common stock purchases may be isolated from
6 trading in preferred shares and in foreign securities.
7 In 1959, the latest year for which such statistics are
8 available, Canadian life insurance companies purchased
9 some \$21 million of Canadian common stocks and sold \$14
10 million, indicating a net inflow that year of \$7
11 million. If British life insurance companies had been
12 included, the total would be somewhat higher.

13 32. From the same source, the market value
14 of life insurance company holdings of Canadian common
15 stocks at December 31, 1959, can also be derived.
16 These amounted to approximately \$145 million for
17 Canadian companies, \$52 million for British companies
18 and zero for other foreign companies, giving a total of
19 \$197 million, or $2\frac{1}{2}$ per cent of total assets. As a
20 matter of general interest, the distribution of assets
21 of life funds in respect of business transacted in the
22 United Kingdom was given in the Radcliffe Report; in
23 1957 common stock holdings represented about 17 per cent
24 and those preferred stocks 7 per cent. As a proportion
25 of the value of Canadian common stocks listed in
26 Canada, these holdings represented 0.98 per cent. (See
27 Table XV below).

28 33. Fire and Casualty Insurance Companies.
29 The market value of stock holdings (common and preferred,
30 Canadian and foreign) of fire and casualty insurance



Report of the Superintendent of Insurance General

estimates; this source has the added virtue that

Canadian common stock purchases may be isolated from

trading in preferred shares and in foreign securities.

In 1959, the latest year for which such statistics are

available, Canadian life insurance companies purchased

some \$21 million of Canadian common stocks and sold \$15

million, indicating a net inflow that year of \$6

million. If British life insurance companies had been

included, the total would be somewhat higher.

32. From the same source, the market value

of life insurance company holdings of Canadian common

stocks at December 31, 1959, can also be derived.

These amounted to approximately \$45 million for

Canadian companies, \$22 million for British companies

and zero for other foreign companies, giving a total of

\$197 million, or 2.5 per cent of total assets. As a

matter of general interest, the distribution of assets

of life funds in respect of business transacted in the

United Kingdom was given in the Radcliffe Report; in

1957 common stock holdings represented about 17 per cent

and those preferred stocks 7 per cent. As a proportion

of the value of Canadian common stocks listed in

Canada, these holdings represented 0.50 per cent. (See

Table XV below).

33. Prime and Canadian Insurance Companies.

The market value of stock holdings (common and preferred

Canadian and foreign) of life and casualty insurance



1 companies at the end of 1959 amounted to approximately
2 \$80 million, representing 3.3 per cent of total assets
3 of \$2.4 billion. While this proportion appears fairly
4 low, from Table V it is apparent that annual net demand
5 has in fact been sizeable, averaging \$7 million annually
6 between 1955 and 1959. A breakdown of stock holdings
7 at the end of 1959, reveal that out of an estimated
8 total of Canadian equities of some \$79 million, common
9 stocks at market value accounted for \$69 million, and
10 preferred stocks \$10 million.

11 34. Trust companies. Trust companies form
12 a most important sector and one for which only limited
13 information is available. The figures of net additions
14 to equity holdings appearing in Table V are based on
15 the book value of company and guaranteed funds. Company
16 funds consist of retained earnings, the proceeds of
17 stock issues and in some cases money borrowed from the
18 chartered banks. Guaranteed funds are made up of
19 deposits, on which checking privileges are available,
20 and guaranteed trust certificates; these latter are debt
21 instruments issued by the trust companies, normally with
22 maturities of one to five years; the element of
23 guarantee is provided by the fact that the trust company
24 is required to set aside cash and eligible securities
25 equal to the aggregate amount of these funds. The
26 relatively short-term nature of such liabilities clearly
27 affects the investment policies that are followed; it
28 may be cited as one reason for the apparent modesty of
29 equity holdings. This is illustrated in the following
30 table.





TABLE VII
Trust Company Assets

As at December 31,	1954 \$ million	%	1959 \$ million	%	1960 \$ million	%
Securities	344	58.5	496	49.7	655	54.1
Bonds	326	55.4	463	46.4	620	51.2
Preferred & common	18	3.1	33	3.3	35	2.9
Mortgages	165	28.1	385	38.6	442	36.5
Other	79	13.4	118	11.7	113	9.4
Total Company & Guaranteed Funds	588	100%	999	100%	1,210	100%
Administered Funds	4,056		6,403		6,829	

Source: Bank of Canada Statistical Summary, May 1961.



1 35. The proportion of the assets representing
2 company and guaranteed funds made up of equities
3 (foreign as well as Canadian) has not displayed any
4 market trend in recent years; Table V points up the
5 modest role the investment of such funds has played as
6 a net source of demand for stocks.

7 36. To keep these findings in perspective,
8 it is important to remember that, as at the end of
9 1960, company and guaranteed funds represented only 15
10 per cent of total trust company funds, 85 per cent
11 being made up of administered funds (estates, trusts
12 and agency funds and safe custody accounts). In fact,
13 the proportion is lower because book value figures of
14 administered assets are seriously understated: some
15 trust companies, for instance, carry stocks at par and,
16 in the case of no par value, common shares arbitrarily
17 assign a value of \$1 a share. The extent of the
18 distortion, however, is unknown; indeed, this is one
19 of the areas where the inadequacy of published
20 information is most striking. Only in the case of
21 pension fund monies managed by trust companies is an
22 asset break-down available; the subject is discussed at
23 some length in the section on pension funds; at the end
24 of 1960, corporate trustee plans (those administered
25 by trust companies and by Investors Mutual) represented
26 somewhat less than one-third of total trustee pension
27 funds and involved assets of \$1.1 billion. Subtracting
28 these from the total of administered funds on that date,
29 there is \$5.7 billion left on which no information is
30 available; as already pointed out, if account is taken



2. The proportion of the assets represented

guaranteed funds with up of equities

(as well as cash) are not displayed any

market trend in recent years; Table V points up the

modest role the investment of such funds has played as

a net source of demand for stocks.

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it is important to remember that, as at the end of

per cent of total trust company funds, 15 per cent

being made up of equities, bonds, stocks, funds

and agency funds and safe custody accounts). In fact,

the proportion is lower because book value figures of

trust companies, for instance, carry stocks at par and

in the case of no par value, common shares are usually

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distortion, however, is unknown; indeed, this is one

of the areas where the lack of publicity of published

information is most striking. Only in the case of

publicly traded issues reported by trust companies is an

asset breakdown available; the subject is discussed at

some length in the section on pension funds; at the end

of 1960, corporate insured plans (less administered

by trust companies and by Insurance Mutual) represented

somewhat less than one-third of total insured pension

funds and involved assets of \$1.1 billion. Subsequent

these from the total or administered funds on that date,

figures; as already pointed out, all accounts taken



1 of the deflated nature of book value figures, the total
2 would be increased substantially. It may be assumed
3 that within this total, common stocks make up a
4 significant proportion; while U.S. experience should
5 not be treated as representative of administered funds
6 in Canada, it is of some interest to note that in 1959
7 personal trust accounts in U.S. banks and trust
8 companies were over 70 per cent invested in equities.

9 37. College and Endowment Funds.

10 Figures on investments of college and
11 endowment funds are published annually by the Boston
12 Fund. At the end of 1961, total assets of 62 U.S.
13 colleges amounted to \$4,399 million, of which \$2,471
14 million or 56 per cent was invested in common stocks,
15 and \$79 million or 1 3/4 per cent in preferred stocks.
16 Information is available on three Canadian universities
17 (McGill, Carleton and Queen's); at the end of 1961
18 their assets totalled \$118.1 million with common stock
19 holdings making up \$49.6 million or 42 per cent of
20 total assets, and preferred holdings \$2.1 million or
21 1 per cent of total assets.

22 38. Mortgage Loan Companies. Book value
23 holdings of preferred and common stocks of mortgage loan
24 companies (including Investors Syndicate of Canada) at
25 the end of December 1960 amounted to \$44 million, making
26 up 5.1 per cent of total assets of \$860 million. In
27 1959 the holdings were \$41 million, out of total assets
28 of \$784 million. On the basis of changes in book
29 values (see Table V), mortgage loan companies, while
30 remaining fairly modest as a net source of demand for



of the delisted nature of book value figures, the total would be increased substantially. It may be assumed that within this total, common stocks make up a significant proportion; while U.S. experience should not be treated as representative of administered funds in Canada, it is of some interest to note that in 1959 personal trust accounts in U.S. banks and trust companies were over 70 per cent invested in equities.

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38. Mortgage Loan Companies. Book value

holdings of preferred and common stocks of mortgage loan companies (including Investors Syndicate of Canada) at the end of December 1960 amounted to \$44 million, making up 5.1 per cent of total assets of \$860 million. In 1959 the holdings were \$41 million, out of total assets of \$734 million. On the basis of changes in book values (see Table V), mortgage loan companies, while remaining fairly modest as a net source of demand for



1 equities, have been more important than trust companies,
2 considering only the investment of company and guaranteed
3 funds.

4 39. Pension Funds. Pension funds form an
5 area of institutional investment which is well
6 documented. They fall into three broad categories:
7 trusted plans (most frequently of trust companies) and
8 annuities, notably those sold by life insurance companies
9 and those by the Government of Canada. The Dominion
10 Bureau of Statistics estimates the assets and reserves
11 of all such pension plans in Canada to have amounted at
12 the end of December, 1960 to \$5,424 million, with the
13 assets of Trusted Pension Plans (book value) accounting
14 for \$3,616 million, those held against Life Insurance
15 Group Annuities in Canada \$1,209 million and against
16 Federal Government Group Annuities \$600 million. In
17 1956, the assets of Trusteed Pension Plans were
18 estimated at \$1,959 million, Life Insurance Group
19 Annuities \$646 million and Federal Government Group
20 Annuities \$930 million.

21 40. Most of the pension plan underwriting
22 by the Government Annuities Branch was done between 1938
23 (the year it started operations) and 1948; new business
24 done since then by the Annuities Branch has been
25 insignificant. The substantial growth of trusteed
26 and insurance company pension plan underwriting can
27 be dated from the immediate post-war years. Changes in
28 the laws governing such investments have also served to
29 stimulate this growth. An amendment passed in 1956
30 to the act governing pension funds in Canada freed



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1 trusteed pension plans from a previous requirement which
2 limited their investments to those legal for insurance
3 companies (including a ceiling of 15 per cent in the
4 proportion of equities). In 1960 the law governing
5 insurance company annuity underwriting was also altered,
6 this same limitation being removed. In recent months
7 a start has been made in Canada in connection with the
8 provision of variable annuities.

9 41. Pension plans vary extensively as to the
10 composition of their assets. The investments held
11 against insurance company annuities cannot be
12 distinguished, in the statistics that are published,
13 from the overall assets of the companies concerned,
14 on which some comment has already been made in an
15 earlier section. It is in the area of trusteed pension
16 plans that the greatest amount of information is
17 available; they are, of course, in terms of size, the
18 most important of the three. The trusteed pension plans
19 dealt with in the 1960 D.B.S. survey of that name are
20 those of a) industry (incorporated companies, partnerships
21 and sole ownerships), b) municipalities and municipal
22 enterprises, c) federal and provincial crown
23 corporations, d) federal and provincial boards and
24 commissions, e) religious and charitable organizations,
25 f) provincial civil service plans for three provinces,
26 g) teachers' federation plans for seven provinces, h)
27 educational institutions and health organizations such
28 as hospitals, i) trade and employee associations, j)
29 co-operatives. Returns from a total of 1,140 funds
30 were used, covering 1,009,127 employees.



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2 limited their investments to those legal for insurance
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4 proportion of equities). In 1960 the law governing
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are available for the year 1960.

TABLE VIII
Trusted Pension Plans of Incorporated Companies

Asset Distribution at Book Value	<u>1952</u>		<u>1956</u>		<u>1960 *</u>		Change 1952-1960 (\$ million)
	(\$ million)	%	(\$ million)	%	(\$ million)	%	
Canadian bonds	603.1	84.1	993.9	77.7	1,555.5	72.6	+ 952.4
Mortgages	29.0	4.0	96.9	7.6	167.4	7.8	+ 138.4
Canadian preferred	51.7	7.2	33.5	2.6	24.5	1.2	+ 187.6
Canadian common			72.8	5.7	214.8	10.0	
Foreign bonds, preferred			2.9	0.2	2.9	0.1	
Foreign common	1.5	0.2	6.0	0.5	23.0	1.1	+ 24.4
Other assets	32.2	4.5	73.7	5.7	154.8	7.2	+ 122.6
Total	717.5	100.0	1,279.8	100.0	2,142.8	100.0	+1,425.3
Canadian common, preferred and foreign common	53.2**	7.4	112.3	8.8	262.3	12.3	+ 209.1

* Also includes partnerships and sole ownerships.

** Includes \$242,000 in foreign bonds.

Sources: D.B.S. Survey of Canadian Trusted Pension Funds 1953, Trusted Pension Plans Financial Statistics 1957, 1960.

Also including preliminary and some outstanding. The figures are \$5,000 in 1954 and \$10,000 in 1955.

THE PRESIDENT OF THE UNITED STATES

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42. Within these various groups, the pension funds for which the longest run of historical information has been published are those of industry. They also happen to be the most important single sector within trustee funds: at the end of 1960, industry plans had a book value of \$2,143 million and accounted for close to 60 per cent of the total of \$3,616 million. In Table VIII the asset distribution (book value) of the plans of incorporated companies is presented for the three years 1952, 1956 and 1960. The very rapid growth in pension plans in Canada during the post-war period is illustrated in the three-fold increase in total assets between 1952 and 1960. For our purposes, the most interesting point that emerges is the even more rapid rise in equity holdings: in 1952 investments in Canadian common and preferred stocks and foreign common stocks amounted to about \$53 million and made up 7.4 per cent of the aggregate portfolio; in 1960, the absolute amount had risen to \$239 million and the proportion to 12.3 per cent. If market values were taken, this percentage would be even higher; figures are not available for 1960, but in 1959 the proportion of assets held in equities at market values amounted to 14.1 per cent against 11.5 per cent in terms of book values.

43. From these figures, it would seem that between 1952 and 1960 there was a net flow of funds of \$209 million, or an annual flow of \$26 million, into the stock market as a result of investment decisions made by the trustees of industry pension plans. If



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43. From these figures, it would seem that between 1952 and 1960 there was a net flow of funds of \$209 million, or an annual flow of \$66 million, into the stock market as a result of investment decisions made by the trustees of industry pension plans. It



foreign equities are excluded, the net inflows come to \$188 million and \$23 million a year. In connection with the calculation of flows of pension money for investment purposes on the basis of book value figures, it is worth noting that, unlike insurance companies, trustee pension funds are under no statutory obligation to value their assets and show a state of complete solvency; this means that they can worry less about temporary declines in market prices and, moreover, that they do not have the incentive that the insurance companies have to write down the book value of their assets.

44. Before leaving the subject of industry funds and particularly their role in the Canadian equity market, special mention should be made of the pooled funds; they are, of course, included in the industry total. As suggested by the name, these funds are set up by trustees for the convenience of small firms whose plans are combined, thereby providing the diversity, security and yield that it would be impossible to obtain if each one were to be managed separately. What is particularly interesting is the rapidity of their growth, as well as the emphasis placed on equities. At the end of December, 1960 pooled pension fund assets (book value) totalled \$93.7 million, an increase of \$30.6 million over the previous year-end, indicating a monthly rate of growth of \$2.5 million. The proportion invested in stocks amounted to 26.5 per cent (22.2 per cent in Canadian common stocks), as against 25.3 per cent at the end of 1959. While it would be wrong



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At the end of December, 1960 pooled pension fund assets

(book value) totalled \$93.7 million, an increase of

\$30.6 million over the previous year-end, indicating

a monthly rate of growth of 2.5 million. The propor-

tion invested in stocks amounted to 26.5 per cent (22.2

per cent in Canadian common stocks), as against 22.3

per cent at the end of 1959. While it was 19.4

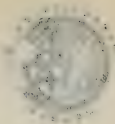


1 to regard the experience of pooled funds as
2 representative of the way in which fresh pension fund
3 money is being invested, it is certainly indicative of
4 a growing interest in equities.

5 45. As pointed out earlier, industry pension
6 plans make up about three-fifths of total trustee
7 pension plans. For recent years, figures are also
8 available for the overall trustee group. These show
9 that at the end of 1960 holdings of Canadian common
10 and preferred stocks at book value came to \$255.1
11 million and \$2713 million respectively (representing
12 7.0 per cent and 0.8 per cent of total assets). What
13 is particularly revealing is the extremely limited
14 nature of equity holdings in the pension funds of crown
15 corporations and government agencies; the bias towards
16 local debt instruments is also striking. The attached
17 Table IX brings out these two points.

18 46. Once again, market value statistics do
19 not go beyond 1959; in that year the market value of
20 Canadian common stocks held by all trustee pension
21 plans totalled \$238.6 million, representing 7.8 per cent
22 of overall assets (as against 4.6 per cent of the book
23 value) and that of Canadian preferred stocks \$29.5
24 million, making up 1 per cent of total assets. As a
25 proportion of the value of Canadian common stocks listed
26 in Canada, these holdings represented 1.16 per cent.
27 (see Table XV).

28 47. In the year 1960, it can be estimated
29 that the net flow of funds into Canadian common stock
30 investment by all trustee pension funds was \$50 million



to regard the experience of pooled funds as representative of the way in which fresh pension fund money is being invested, it is certainly indicative of a growing interest in equities.

45. As pointed out earlier, industry pension plans make up about three-fifths of total trustees pension plans. For recent years, figures are also available for the overall trustees group. These show that at the end of 1960 holdings of Canadian common and preferred stocks at book value came to \$255.1 million and \$271.3 million respectively (representing 7.0 per cent and 0.6 per cent of total assets). What is particularly revealing is the extremely limited nature of equity holdings in the pension funds of crown corporations and government agencies; the bias towards local debt instruments is also striking. The attached Table IX brings out these two points.

46. Once again, market value statistics do not go beyond 1959; in that year the market value of Canadian common stocks held by all trustees pension plans totalled \$238.6 million, representing 7.6 per cent of overall assets (as against 7.0 per cent of the book value) and that of Canadian preferred stocks \$29.5 million, making up 1 per cent of total assets. As a proportion of the value of Canadian common stocks listed in Canada, these holdings represented 1.16 per cent. (see Table XV).

47. In the year 1960, it can be estimated that the net flow of funds into Canadian common stock investment by all trustees pension funds was \$50 million

TABLE IX

1959
Selected Trusteed Pension Plans

Investments at Market Values	Municipalities & Municipal Enterprises		Provincial Crown Corps. & Govt. Agencies		Fed. Crown Corps. & Govt. Agencies		Religious & Charitable		Educational	
	(\$ million)	%	(\$ million)	%	(\$ million)	%	(\$ million)	%	(\$ million)	%
Federal Govt. bonds	14.7	8.4	52.2	17.3	123.5	32.6	5.0	12.2	9.7	3.2
Provincial bonds	32.3	18.3	209.7	69.7	105.7	27.9	9.1	22.0	255.5	75.0
Municipal bonds	87.8	49.8	19.4	6.5	2.3	0.6	8.7	21.0	25.1	8.4
Canadian common stocks	5.1	2.9	.3	0.1	18.2	4.8	2.9	7.1	.5	0.2
Other investments	36.4	20.6	19.2	6.4	129.4	34.1	15.6	37.7	9.8	3.2
Total	176.3	100.0	300.8	100.0	379.1	100.0	41.3	100.0	300.6	100.0

Source: D.B.S. Trusteed Pension Plans, Financial Statistics, 1959.

1900

1901

1902

Year	1900		1901		1902		1903		1904		1905		1906		1907		1908		1909		1910		1911		1912		1913		1914		1915		1916		1917		1918		1919		1920		1921		1922		1923		1924		1925		1926		1927		1928		1929		1930		1931		1932		1933		1934		1935		1936		1937		1938		1939		1940		1941		1942		1943		1944		1945		1946		1947		1948		1949		1950		1951		1952		1953		1954		1955		1956		1957		1958		1959		1960		1961		1962		1963		1964		1965		1966		1967		1968		1969		1970		1971		1972		1973		1974		1975		1976		1977		1978		1979		1980		1981		1982		1983		1984		1985		1986		1987		1988		1989		1990		1991		1992		1993		1994		1995		1996		1997		1998		1999		2000		2001		2002		2003		2004		2005		2006		2007		2008		2009		2010		2011		2012		2013		2014		2015		2016		2017		2018		2019		2020		2021		2022		2023		2024		2025		2026		2027		2028		2029		2030		2031		2032		2033		2034		2035		2036		2037		2038		2039		2040		2041		2042		2043		2044		2045		2046		2047		2048		2049		2050		2051		2052		2053		2054		2055		2056		2057		2058		2059		2060		2061		2062		2063		2064		2065		2066		2067		2068		2069		2070		2071		2072		2073		2074		2075		2076		2077		2078		2079		2080		2081		2082		2083		2084		2085		2086		2087		2088		2089		2090		2091		2092		2093		2094		2095		2096		2097		2098		2099		2100		2101		2102		2103		2104		2105		2106		2107		2108		2109		2110		2111		2112		2113		2114		2115		2116		2117		2118		2119		2120		2121		2122		2123		2124		2125		2126		2127		2128		2129		2130		2131		2132		2133		2134		2135		2136		2137		2138		2139		2140		2141		2142		2143		2144		2145		2146		2147		2148		2149		2150		2151		2152		2153		2154		2155		2156		2157		2158		2159		2160		2161		2162		2163		2164		2165		2166		2167		2168		2169		2170		2171		2172		2173		2174		2175		2176		2177		2178		2179		2180		2181		2182		2183		2184		2185		2186		2187		2188		2189		2190		2191		2192		2193		2194		2195		2196		2197		2198		2199		2200		2201		2202		2203		2204		2205		2206		2207		2208		2209		2210		2211		2212		2213		2214		2215		2216		2217		2218		2219		2220		2221		2222		2223		2224		2225		2226		2227		2228		2229		2230		2231		2232		2233		2234		2235		2236		2237		2238		2239		2240		2241		2242		2243		2244		2245		2246		2247		2248		2249		2250		2251		2252		2253		2254		2255		2256		2257		2258		2259		2260		2261		2262		2263		2264		2265		2266		2267		2268		2269		2270		2271		2272		2273		2274		2275		2276		2277		2278		2279		2280		2281		2282		2283		2284		2285		2286		2287		2288		2289		2290		2291		2292		2293		2294		2295		2296		2297		2298		2299		2300		2301		2302		2303		2304		2305		2306		2307		2308		2309		2310		2311		2312		2313		2314		2315		2316		2317		2318		2319		2320		2321		2322		2323		2324		2325		2326		2327		2328		2329		2330		2331		2332		2333		2334		2335		2336		2337		2338		2339		2340		2341		2342		2343		2344		2345		2346		2347		2348		2349		2350		2351		2352		2353		2354		2355		2356		2357		2358		2359		2360		2361		2362		2363		2364		2365		2366		2367		2368		2369		2370		2371		2372		2373		2374		2375		2376		2377		2378		2379		2380		2381		2382		2383		2384		2385		2386		2387		2388		2389		2390		2391		2392		2393		2394		2395		2396		2397		2398		2399		2400		2401		2402		2403		2404		2405		2406		2407		2408		2409		2410		2411		2412		2413		2414		2415		2416		2417		2418		2419		2420		2421		2422		2423		2424		2425		2426		2427		2428		2429		2430		2431		2432		2433		2434		2435		2436		2437		2438		2439		2440		2441		2442		2443		2444		2445		2446		2447		2448		2449		2450		2451		2452		2453		2454		2455		2456		2457		2458		2459		2460		2461		2462		2463		2464		2465		2466		2467		2468		2469		2470		2471		2472		2473		2474		2475		2476		2477		2478		2479		2480		2481		2482		2483		2484		2485		2486		2487		2488		2489		2490		2491		2492		2493		2494		2495		2496		2497		2498		2499		2500		2501		2502		2503		2504		2505		2506		2507		2508		2509		2510		2511		2512		2513		2514		2515		2516		2517		2518		2519		2520		2521		2522		2523		2524		2525		2526		2527		2528		2529		2530		2531		2532		2533		2534		2535		2536		2537		2538		2539		2540		2541		2542		2543		2544		2545		2546		2547		2548		2549		2550		2551		2552		2553		2554		2555		2556		2557		2558		2559		2560		2561		2562		2563		2564		2565		2566		2567		2568		2569		2570		2571		2572		2573		2574		2575		2576		2577		2578		2579		2580		2581		2582		2583		2584		2585		2586		2587		2588		2589		2590		2591		2592		2593		2594		2595		2596		2597		2598		2599		2600		2601		2602		2603		2604		2605		2606		2607		2608		2609		2610		2611		2612		2613		2614		2615		2616		2617		2618		2619		2620		2621		2622		2623		2624		2625		2626		2627		2628		2629		2630		2631		2632		2633		2634		2635		2636		2637		2638		2639		2640		2641		2642		2643		2644		2645		2646		2647		2648		2649		2650		2651		2652		2653		2654		2655		2656		2657		2658		2659		2660		2661		2662		2663		2664		2665		2666		2667		2668		2669		2670		2671		2672		2673		2674		2675		2676		2677		2678		2679		2680		2681		2682		2683		2684		2685		2686		2687		2688		2689		2690		2691		2692		2693		2694		2695		2696		2697		2698		2699		2700		2701		2702		2703		2704		2705		2706		2707		2708		2709		2710		2711		2712		2713		2714		2715		2716		2717		2718		2719		2720		2721		2722		2723		2724		2725		2726		2727		2728		2729		2730		2731		273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(of which close to \$40 million by industry pension plans); at the same time, there was a net outflow on account of Canadian preferred stocks of \$4 million; net investments in bonds and mortgages amounted to about \$350 million. This compares with a gross cash flow in 1960 for all trustee pension plans of \$555 million, \$393 million representing employer and employee contributions and the rest almost entirely investment income. With expenditures at \$154 million (\$108 million being pension payments out of funds), the net cash flow in 1960 was somewhat more than \$400 million. This would indicate that on average 12 per cent of net funds available for investment is going into Canadian equities.

48. Investment Companies.

From Table V it appears that mutual funds have been easily the most important domestic source of demand for equities in the period covered. In the following table, information is presented on resident-owned investment funds, that is to say, in addition to mutual funds, closed-end funds provided they are largely owned in Canada and excluding Power Corporation and Argus Corporation.

49. While a break-down of investments at book value is not readily available, it may be estimated that in 1959 the net flow of funds into Canadian common stocks amounted to around \$80 million. In this connection, of course, the open-end mutual funds are of major importance; the closed-end funds are only significant to the extent that the proportions of their portfolios are switched between equities and debt, or



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Table X

Investment Companies' Assets

	1955	1956	1957	1958	1959	1960
(Market value)			(million dollars)			
Total Bonds	52	62	84	93	112	140
Total Stocks	405	448	400	520	583	598
of which preferred	44	56	55	52	47	54
Canadian common	284	323	287	425	472	467
foreign common	76	69	58	43	64	78
Total Investments	456	509	485	614	695	737
Total investments at book value	325	399	444	478	592	653



X 1675.1

[illegible]



1 because new money has become available for investment as
2 a result of fresh financing. At the end of 1959, with
3 the market value of Canadian common stocks at \$472
4 million, holdings made up approximately 2.28 per cent
5 of the value of Canadian common stocks listed at the
6 time. (see Table XV).

7 50. Foreign Investment.

8 Since the end of the war, Canada has been by
9 far the world's largest importer of private long-term
10 capital; this has taken the form both of debt and equity
11 capital. As indicated earlier, the extent of foreign
12 ownership of Canadian enterprises is an important factor
13 limiting the supply of Canadian common stocks.

14 51. The figures in Table XI cover both direct
15 investment, defined to include concerns which are known
16 to have 50 per cent or more of their voting stock held
17 in one country outside Canada, and portfolio investments,
18 covering enterprises where the holdings are minority in
19 character. The fact that the percentages relate to cap-
20 ital employed and that they cover also direct investment
21 taking the form of wholly-owned subsidiaries means that
22 it is impossible to make precise statements, on the
23 basis of this table, regarding the extent of foreign
24 ownership of Canadian common stocks in certain
25 industries. It does, however, provide a fair indication
26 of the areas where this is heaviest. At the end of 1959
27 the book value of the capital stock of Canadian companies
28 owned by non residents amounted to \$9,916 million, of
29 which \$7,117 million in the United States. Of these
30 totals, direct investment accounted for \$7,324 million



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TABLE XI
Non-Resident Ownership in Selected Canadian Industries

	Total Non-Resident Ownership		of which by U.S. Residents	
	1948	1954	1948	1959
Manufacturing	42%	47%	35%	41%
Petroleum & natural gas	-	60	-	57
Mining & smelting	39	53	32	50
Railways	45	35	21	9
Other utilities	20	14	16	12
Total of above plus merchandising	32	32	23	26

Note: The table describes the proportions of non-resident ownership of the capital employed in selected industries.

Source: D.B.S. The Canadian Balance of International Payments, 1960.



Source: D.T. 10. The Commerce Bureau of Industrial Resources, 1940.

The capital employed in selected industries.

Note: The table presents the percentage of non-Resident ownership in selected industries.

	35	35	43	33	32	30
merchandise						
total of above plus						
unclassified						
Other utilities	50	41	21	10	15	15
Business	42	32	15	12	2	2
Mining & smelting	30	23	22	35	14	20
Chemical & allied	-	20	23	-	12	12
Manufacturing	424	274	212	322	342	414
Transportation & communication	124	122	122	124	122	122

Non-Resident Ownership in Selected Consumer Industries

TABLE 11

1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30



1 and \$5,922 million respectively.

2 52. Additional information is also available
3 on international trade in outstanding Canadian stocks,
4 as distinct from investment flows arising from the
5 flotation of new issues. In Table XII results since
6 1952 are presented; a positive figure indicates a net
7 inflow of capital into Canada as a result of the sale
8 to non-residents of either Canadian or Canadian-held
9 foreign stocks. The figures, of course, provide no
10 indication of the gross volume of international trans-
11 actions; that these can be very large is indicated in
12 estimates made by the D.B.S. according to which gross
13 sales to non-residents of outstanding issues of Canadian
14 common stocks in 1959 accounted for somewhat more than
15 one-fifth of the value of the shares traded on the
16 principal exchanges in Canada that year.

17 53. In Table V, estimates are given of the
18 net investment flows into stocks of N.R.O. Funds and
19 "other foreign portfolio investments". That they do
20 not correspond to the figures presented in Table XII may
21 be largely explained by the fact that Table V includes
22 purchases of new issues. From the statistics presented
23 in Table V, it is interesting to note that in the period
24 1955-1959 the combined stock purchases of N.R.O. funds
25 and "other foreign portfolio investments" amounted to
26 \$887 million, and that those of the Canadian institutions
27 covered in the table came to \$555 million. While the
28 incomplete nature of the figures on Canadian institutional
29 buying has to be taken into account, the size of foreign
30 buying in both absolute and relative terms is neverthe-



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1955-1959 the combined stock purchases of N.R.O. Funds

and "other foreign portfolio investments" amounted to

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covered in the table came to \$552 million. While the

incomplete nature of the figures on Canadian institutions

buying has to be taken into account, the size of foreign

buying in both absolute and relative terms is neverthe-

TABLE XII

Trade in Outstanding Securities Between Canada and other Countries

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1952-1961
.....Net capital movements in millions of dollars.....											
Canadian Stocks	+ 72	+ 21	+ 129	+ 138	+ 183	+ 137	+ 88	+ 110	+ 49	+ 40	+ 972
of which with U.S.A.	+ 66	+ 5	+ 87	+ 92	+ 69	+ 5	+ 70	+ 75	+ 54	+ 120	+ 643
with U.K.	- 6	+ 7	+ 20	+ 28	+ 72	+ 87	+ 4	+ 7	- 16	- 61	+ 141
with all others	+ 12	+ 9	+ 22	+ 18	+ 47	+ 45	+ 14	+ 28	+ 11	- 19	+ 187
Foreign Stocks (U.S.)	+ 9	+ 12	+ 6	+ 26	+ 8	+ 47	+ 10	- 24	- 2	- 5	+ 87

Note: Prior to 1956, the U.K. figures also cover trade with other sterling area countries.

Source: D.B.S. Sales and Purchases of Securities between Canada and other countries.

APPENDIX

Table showing the results of the analysis of the data for the various cases.

Case	1921	1922	1923	1924	1925	1926	1927	1928	1929	1930	1931	1932	1933	1934	1935	1936	1937	1938	1939	1940
1	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
2	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
3	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
4	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
5	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
6	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
7	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
8	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
9	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10
10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10	10

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2 54. In order to provide a balanced view of
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5 the opportunity to purchase stock in an enterprise that
6 was previously a wholly-owned subsidiary of a foreign
7 firm. Greyhound Lines of Canada is a case in point;
8 formerly wholly owned by The Grehound Corporation of the
9 U.S., in 1958, 20 per cent of its 900,000 common shares
10 to be outstanding were offered to the public. More
11 recently, Esquisite Form Brassiers Canada-Ltd.,
12 subsidiary of the U.S. firm, Equisite Form Brassiers Inc.
13 was reorganized as a public company and, in January,
14 1961, a public stock offering of convertible preferred
15 and common, equivalent to nearly 50 per cent of the
16 equity capitalization, was made. At the time, the
17 president of the parent firm said that the move
18 represented an effort to comply with the wishes of the
19 Canadian Government, which has been urging U.S.
20 companies to make stock in their Canadian subsidiaries
21 available to Canadians. As another example of a company
22 the ownership of which has been repatriated to Canada,
23 mention may be made of Metropolitan Stores of Canada.

24 55. Before leaving the subject of foreign
25 ownership, it is clearly necessary to mention Canadian
26 ownership of foreign assets. At the end of 1959 total
27 direct investment amounted to \$2,309 million; if the
28 equity of non-residents in Canadian assets abroad is
29 taken into consideration, the figure is reduced by
30 about \$1 billion. At the same date, the book value of



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TABLE XIII

Non-Resident Control in Selected Industries

	Total Non-Resident Control		of which by U.S. Residents	
	1948	1954	1948	1954
Manufacturing	43%	51%	39%	42%
Petroleum & Natural Gas	-	69	-	67
Mining and smelting	40	51	37	49
Railways	3	2	2	2
Other utilities	24	8	24	7
Total of above plus merchandising	25	28	22	24
				26

Note: In calculating control, the total book value is taken of capital employed in companies in which generally 50 per cent or more of the voting stock is known to be held in one country outside Canada. For 1948, petroleum and natural gas is included in the other industries listed.

source: D.B.S. The Canadian Balance of International Payments, 1960.

Balance, 1960

Source: D.B.2. The Canadian Balance of International

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capital employed in companies in which generally 50 per
Note: In calculating control, the total stock value is taken of

	US	85	35	55	45	50
merchandise						
rest of above plus						
Other activities	45	8	2	45	7	4
Residual	3	5	5	5	5	5
Wholesale and retail	40	15	10	35	40	23
Belgium & Ireland	-	60	12	-	12	60
Manufacturing	40	25	25	30	45	44
	100	100	100	100	100	100
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Table XIII

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10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26 27 28 29 30



1 portfolio investments came to \$1,141 million, of which
2 \$892 million in stocks.

3 56. A final consideration is that of foreign
4 control, as distinct from ownership. While this
5 clearly has particular relevance to matters of policy,
6 and less to a discussion of the available supply of
7 Canadian equities, it is convenient to treat the question
8 briefly at this point. It may be noted that in several
9 cases, the degree of control exceeds that of ownership.

10 57. During the period under review, there
11 has been a consistent rise in the proportions of the
12 manufacturing, oil, natural gas, mining and smelting
13 industries controlled abroad, very largely in the United
14 States, while there has been a steady decline in the
15 importance of the role of foreign investors in railroads
16 and utilities; this latter development reflects in part
17 the growth that has taken place in government-owned
18 railroads and hydro-electric installations.

19 58. In interpreting these statistics, it
20 should be remembered that the industries chosen are
21 precisely those in which foreign participation is
22 especially important. There are in fact large areas
23 of the economy where foreign investment is insignificant,
24 as, for instance, in agriculture, residential
25 construction and merchandising, while in manufacturing
26 Canadian control predominates in textiles, clothing,
27 ~~beverages~~, many kinds of food processing and primary iron
28 and steel.

29 59. Direct foreign investment in Canada has
30 usually been in response to at least one of three goals;



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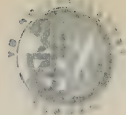
58. In interpreting these statistics, it should be remembered that the industries chosen are precisely those in which foreign participation is especially important. There are in fact large areas of the economy where foreign investment is insignificant, as, for instance, in agriculture, residential construction and merchandising, while in manufacturing Canadian control predominates in textiles, clothing, many kinds of food processing and primary iron and steel.

59. Direct foreign investment in Canada has usually been in response to at least one of three goals:



1 access to the Canadian market, access to the
2 Commonwealth market or the exploitation of Canadian
3 natural resources; this third aspect of foreign invest-
4 ment has either involved manufacturing in Canada and
5 subsequent export of the finished goods, as in the case
6 of newsprint, or, more commonly, shipment abroad of
7 commodities in a semi-processed or primary form, of
8 which iron ore, base metals and a number of other
9 minerals are examples. In all three cases, it may be
10 argued that without massive foreign participation, much
11 of the investment would never have occurred, and that the
12 costs of the investment that might have taken place
13 would probably have been higher. The exploitation of
14 less accessible resources and the growing complexity of
15 modern productive processes are two developments which
16 have tended to emphasize the privileged position of
17 those foreign investors who have ready access to
18 plentiful and comparatively cheap sources of capital.
19 In addition, the rapid advances made since the war in
20 science have served to increase considerably the
21 technological requirements of industry, with the result
22 that even if the savings had been available in Canada
23 to finance these expenditures many of the necessary
24 skills would have been lacking. The technological
25 contribution by non-residents to Canadian growth is
26 impossible to assess exactly, but it has undoubtedly been
27 one of the most valuable features of foreign investment.

28 60. While recognizing these factors, it is
29 nevertheless true that the existence of a large measure
30 of such external control must lead to doubts as to



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whether Canadian industry will in all cases be operated in the best interests of Canada. This point was raised in the submission made by the Investment Dealers Association to the Royal Commission on Canada's Economic Prospects. Fears have been expressed that the Canadian economy is being tied too closely to that of the United States in a subsidiary capacity, that this connection may lead to excessive economic fluctuations in Canada, and that profitable opportunities for economic expansion may be neglected or deferred due to control of Canadian resources by foreign interests; for instance, subsidiaries of U.S. companies may be prevented from tapping export markets, which are reserved for the parent companies. While these fears appear at the moment to have little real justification, nevertheless it is in the best national interest for Canada to encourage the maximum domestic ownership and control of the Canadian economy. It is desirable for political as well as economic reasons that Canadians have a feeling of full participation in the development of the country.

61. SUMMARY

In concluding this discussion of the demand for and supply of Canadian common stocks, it may be useful to summarize some of the necessarily tentative findings. In Table XIV, rough estimates are given of the net purchases of Canadian common stocks from certain institutional sources.



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1990年12月1日 星期一 1990年12月1日 星期一



TABLE XIV

Net Purchase of Canadian Common Stocks
in 1959

Million Dollars

Trusteed Pension Funds	\$ 53
Life Insurance Companies, Canadian	11
Resident-owned Investment Funds	77
N.R.O. Funds	-10

62. These few figures are no more than a qualification to Table V, the main weakness of which is the mixing of preferred and common, foreign and Canadian equities. As a general comment, the supply of new Canadian equities may be considered to have been fairly limited in much of the post-war period, when viewed in the light of the economic expansion Canada has witnessed.

63. It is apparent from Table V, however, that, in relation to this supply, demand from selected institutional investors and from abroad has been heavy: in the period 1955-59, it was equivalent to three-fifths of new stock issues. That this buying has been concentrated on a limited list of Canadian issues is very roughly illustrated in information available on common stock holdings of Canadian and U.S. investment companies (excluding Power Cor. and Argus). In mid-1961 such companies had holdings of more than 15 per cent of the outstanding shares of Alberta Gas Trunk, Calgary & Edmonton, Calgary Power, Canadian Export Gas, Cassiar Asbestos, Gatineau Power, Greater Winnipeg Gas, Simpsons and Union Gas. Investments representing

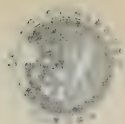


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1 more than 10 per cent of the outstanding common shares
2 included Atlas Steels, Dominion Foundries & Steel,
3 Industrial Acceptance Corporation, Loblaw "A", Moore
4 Corporation and Zeller's. When it is remembered that
5 these proportions concern only investment company
6 holdings, the concentration of institutional interest
7 on a relatively short list of "blue chip" stocks becomes
8 apparent. A further consideration is that where
9 control is held in a limited number of hands, the supply
10 of stock that is potentially available for trading is
11 much reduced. Zeller's is an example, with W.T. Grant
12 having a 51 per cent interest.

13 64. There are several reasons for believing
14 that this institutional demand has risen since 1959
15 and may strengthen further. In recent years, for
16 instance, several obstacles to stock ownership have been
17 removed: the relaxation of investment restrictions
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19 the acts governing the operations of insurance companies
20 which have permitted the sale of variable annuities
21 are cases in point; the importance of equities in the
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23 In addition, a number of fresh incentives to the
24 ownership of stocks have been created, some directed
25 solely towards Canadian equities. As a result of
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28 investment companies must obtain at least three-quarters
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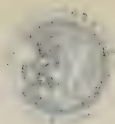
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1 to qualify for tax exemption, they must derive 90 per
2 cent of their investment income from Canadian sources;
3 in both cases these targets have to be reached by
4 December, 1963.

5 65. In Table XV, the importance of several
6 institutions in the Canadian market at the end of 1959
7 is indicated; comparisons are made with similar groups
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10 It must first be recognized that the figures are
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12 being perfect; the U.S. statistics, for instance,
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15 in the two countries are as of different dates.....But
16 these qualifications should not invalidate the general
17 finding that equities form a much smaller proportion
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24 financial intermediaries that is weak in comparison
25 with the experience of Americans.

26 66. Recommendations of increased equity
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29 equities. In a world increasingly characterized by
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TABLE XV

Institutional Stock Holdings in Canada and the United States

Canadian Financial Institutions.....		United States Financial Institutions.....		
	Holdings of Canadian		As %	Holdings of Equities		As %
	Common Stocks at Mkt. Value (Dec. 31, 1959; \$ million)	Assets	Stock Market A B	at Mkt. Value Dec. 31, 1960; \$ million	Total Assets	N.Y.S.E. List
Trusteed pension funds	\$ 239	8%	1.16%	\$ 14,600	44%	3.76%
Life insurance companies	197	2½	0.96	5,000	4	1.29
Fire & casualty ins. companies	70	6	0.29	9,000	30	2.32
Investment funds (resident-owned)	472	68	2.28	14,000	70	3.61
Non-resident-owned (NRO)	331	90	1.60	-	-	-
Trust accounts with banks and trust companies	N.A.	-	-	37,200	73	9.59
Total listed	1,300	-	6.28	79,800	-	20.53

Notes: A: valued at \$20.7 billion being the value of stocks listed on the Toronto Stock Exchange at December 31, 1959, less preferred shares, less U.S. shares, less "penny" mining shares, plus investment grade common stocks only listed in Montreal.

B: valued at \$14.5 billion being the same as A less 30% being the estimated proportion of stocks owned on a permanent basis (viz. Inter-company holdings) - and in effect untradeable.

* Valued at \$387.8 billion.

N.B. Nearly all figures in this table are approximations.

Sources: Canadian sources have been listed in the preceding text. U.S. sources include "Institutional Investing" by Richard W. Lambourne, Financial Analysts, Nov. - Dec. 1961.

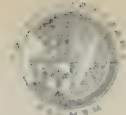


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2 this trend. At the same time, it seems highly
3 desirable that maximum opportunities be provided for
4 investment in Canadian institutions. This may take the
5 form of rendering Canadian stocks more attractive by the
6 removal of certain competitive disadvantages under
7 which Canadian firms operate in relation to foreign
8 companies. In oil and natural gas exploration,
9 development and production for instance, the income tax
10 position of a Canadian corporation or individual is not
11 as favourable as is that of an American corporation or
12 individual. There are of course many other measures
13 that would help to channel investment funds into
14 Canadian equities. As an example of imaginative action
15 in this connection, in Australia, a tax scheme has been
16 evolved permitting an Australian to deduct from his
17 income tax that amount which he can show evidence of
18 having invested in the shares of new companies
19 incorporated for the purpose of exploring for oil.

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22 67. INVESTMENT MANAGEMENT ROLE IN THE
23 CANADIAN ECONOMY

24 In the discussion so far, attention has been
25 drawn on the need to broaden domestic ownership of
26 equities in Canada. Investment dealers and counsellors
27 are very conscious of this and, in their role as port-
28 folio managers, they have done much to improve the
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7. INVESTMENT MANAGEMENT ROLE IN THE CANADIAN ECONOMY

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1 brought about not only by the demands for sophisticated
2 information on the part of institutional investors but
3 also by the expanding needs of individual investors.
4 On the one hand there has been the desire of the
5 professional investor for more detailed and accurate
6 information concerning companies and their public
7 offerings of securities. Improved communication
8 facilities, broader coverage by daily newspapers and
9 periodicals have stimulated a greater desire on the
10 part of the individual investor for specific advice and
11 information.

12 68. The pressure exerted on investment
13 dealers for improved investment management advice is to
14 be explained in part by the background of the men
15 assuming senior positions during the past five to ten
16 years within the investing institutions. In the period
17 prior to the war they did little or no recruiting and,
18 perforce, during the war years it was virtually
19 impossible for them to expand their personnel.
20 Subsequent to the war, a much higher percentage of more
21 highly trained people, such as university graduates,
22 were absorbed into the investing institutions. In
23 addition, the increasing appeal of mutual funds and
24 more planned investment of personal funds created
25 greater opportunities within the industry. These highly
26 trained people sought better sources of information on
27 issues which were being offered by corporations,
28 governments, etc., and this created an enlarged demand
29 for the investment management facilities in Canada.
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7 of people. Indeed, the task of investment management may
8 be said to have attained professional status.

9 69. It might be helpful to list the various
10 types of investors who require, either on a regular or
11 on an intermittent basis, advice concerning their
12 investments:

13 Estates

14 Trusts

15 Personal Accounts

16 Investment Trusts

17 Mutual Funds

18 Pension Funds

19 Corporate Accounts

20 The type of service ranges from the determination of an
21 overall investment policy to the provision of specific
22 information on particular issues making up a portfolio.

23 70. The relationship of an investment counsel
24 or investment manager to the investor is personal and
25 confidential. Such factors as family obligations,
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- Insurance Companies
- Investment Firms
- Mutual Funds
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1 demands on capital and income, actuarial return, etc.,
2 must be considered.

3 71. So much for the background of investment
4 management and its relationship to the investor. The
5 ideal investment is one offering a high rate of return,
6 a good prospect of capital appreciation, a minimal risk
7 of capital loss, and no difficulty about converting back
8 to cash rapidly. It is very hard to find such an
9 investment in the real world. The typical investment
10 problem, therefore, is assigning relative orders of
11 importance to these different criteria. The problem
12 is always difficult because almost all investors are
13 interested, to some extent, in each one of these
14 advantages. Spectacular profits may be achieved through
15 lucky speculation, and protection, nominally guaranteed
16 through the purchase of "riskless" securities, may prove
17 mythical when subjected to deteriorating dollar values.

18 72. At times, certain securities may appear
19 relatively unattractive; at other times it may be
20 advisable to modify the emphasis of some holdings, so
21 that the balance between fixed income investments on
22 the one hand and equity on the other may be shifted.
23 The basic framework is devised in order to give due
24 weight to the degree of protection required, the amount
25 of risk which can be accepted and the need for income.
26 Individual securities are selected with due regard to
27 the preference of an investor for certain industries.

28 73. The securities in question can only be
29 chosen after their merits have been carefully weighed
30 by people highly trained in this type of research work.



1 demands on capital and income, substantial return, etc.,
2 must be considered.
3 71. So much for the background of investment
4 management and its relationship to the investor. The
5 ideal investment is one offering a high rate of return,
6 a good prospect of capital appreciation, a minimal risk
7 of capital loss, and no difficulty about converting back
8 to cash rapidly. It is very hard to find such an
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1 It is necessary for a firm, supplying investment counsel
2 information, to maintain a research department devoted
3 to a continuous, impartial and, perforce, relatively
4 successful analysis of given situations. In certain
5 instances, firms will emphasize certain types of
6 securities and confine their research efforts to those
7 particular areas, but firms which offer a comprehensive
8 investment management service must cover a broad field
9 in Canada. This comprises extractive industries,
10 secondary and primary manufacturing industries, and
11 service organizations. It requires the training and
12 development of competent personnel, who must have
13 adequate educational background to give them the ability
14 to collate and classify the appropriate material.

15 74. It has been estimated that to bring a
16 college or university graduate to the status of a
17 recognized analyst takes a period between four to six
18 years. This indicates that a firm must make a fairly
19 sizeable capital investment in an individual in order
20 to bring him to the point where he can be useful in
21 research. Figures in themselves are not conclusive, but
22 it would seem that a fair estimate is that a capital
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26 further, and assuming that, over a five-year period, a
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1 provide the basis for successful investment or portfolio
2 management.

3 75. The training, either on a permanent or
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5 capital costs of maintaining adequate research
6 facilities. There are substantial capital outlays for
7 the production of informative services, involving, for
8 instance, the use of consultants in a particular field,
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10 it is not only desirable but necessary to provide
11 facilities for the research staff to make extensive field
12 trips to the industries and companies whose activities
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15 short-term or long-term basis. Finally, it is vital
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18 appreciation of world trends, etc. This is a costly and
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20 in proportion to the coverage desired.

21 76. It might be pointed out in conclusion
22 that, where investment management or portfolio advice
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77. THE IMPORTANCE OF CORPORATE PUBLIC
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With the best will in the world, investment dealers and counsellors would have great difficulty making sophisticated judgments on individual securities without the co-operation of the companies concerned. Indeed, competent reporting to shareholders and to the public at large is indispensable. Remarkable progress has been achieved in this respect during the past three decades, and some Canadian companies are among the leaders in the public relations field on this continent; a few of them have figured prominently in the list of trophies awarded for best annual reporting.

78. On the other hand, one must recognize that many Canadian corporations are not giving to the public, holding their shares, the information to which they are entitled. While it is hard to outline a fixed set of rules, it would seem that once a year at least, on the occasion of the annual report, shareholders should be given as complete factual, pictorial and graphic information about the company as possible. This should include interpretation of the company's activities and policies in relation to conditions within its industry, the information being presented in such a way as to afford easy comparison with previous performance. The publication of sales figures, in this connection, is most desirable. In order to make it meaningful for the average shareholders, the report should be written in layman's language, with clear explanations of technical financial terms.



Wales
Dominion of Wales

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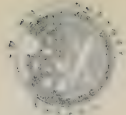
79. Preferably, information given to shareholders should not be limited to the annual report. Interim statements, on a quarterly or semi-annual basis, are highly desirable and these should carry concise information on events affecting the company during the period covered by the interim report. Speeches made by the Chairman or the President at the annual meetings as well as answers given on that occasion to shareholders' questions should also be part of the informative material supplied annually to shareholders. It is also important that each company sees to it that any information pertaining to its activity, capitalization, earnings or dividends, which could materially affect the performance of the shares on the stock exchange, be given as early and as clearly as possible, and with wide and simultaneous distribution.

80. The challenge of gaining investors' confidence through sound public relations policies is a substantial one, but so are the rewards of communication with an audience of growing importance.

81. INVESTMENT CLUBS IN CANADA

In discussing efforts made to broaden stock ownership one must mention investment clubs, in view of the important part they are playing, with the help of members of the Investment Dealers Association, in educating the small investor.

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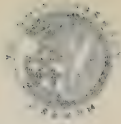
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12 of the clubs have come into being in the past three
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- 15 a) To provide their members with
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17 securities so as to broaden their
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19 b) At the same time to enable them
20 to make their personal savings work.

21 83. In many instance, for two or three years
22 the amounts of capital available for investment are
23 minute. This means that transactions effected by these
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25 their investments, are confined to very small lots of
26 stocks. It is an accepted fact that the odd-lot
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1 business will develop on a large enough scale to offset
2 these losses.

3 84. CO-OPERATION BETWEEN STOCK EXCHANGES
4 INVESTMENT DEALERS ASSOCIATION

5 Much of the public financing of Canada's
6 post-war expansion has been done through Investment
7 Dealers Association members across Canada.

8 85. In the case of equities, the value of
9 listing on a stock exchange as a means of providing a
10 known and ready market has been decisively demonstrated.
11 This has made for closer co-operation between Investment
12 Dealers Association members and the stock exchanges than
13 existed in earlier periods of Canadian development, when
14 equities were not as widely held by the public.

15 86. At the same time, the major stock
16 exchanges have been improving their communication and
17 reporting facilities in order to meet the public's
18 desire for a wider diversification of issues for
19 investment. It was almost mandatory that the stock
20 exchanges across Canada should use every means possible
21 to develop in an harmonious manner their relations with
22 underwriters across Canada, who were instruments in
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24 stock exchanges in Canada have, over the past ten years,
25 each in their own sphere, taken the initiative to
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DEALERS ASSOCIATION AND INVESTMENT TRADING ASSOCIATION

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8 believe that the complementary nature of the functions
9 of the underwriter and the broker are much more clearly
10 defined now in virtue of the co-operation that now
11 exists.

12 87. CONCLUSIONS AND RECOMMENDATIONS

13 (a) In this discussion, a recurring theme has
14 been the inadequacy of the available statistical
15 material. Such shortcomings are glaring in the case
16 of the investment of funds administered by trust
17 companies. It is recommended that the Dominion Bureau
18 of Statistics give high priority to having the relevant
19 material assembled and published.

20 (b) On the basis of those statistics that
21 are available, it appears that the proportion of
22 individuals in Canada owning stocks is not very
23 different from that in the United States; this may be in
24 part due to the incentive to stock holding provided by
25 the 20 per cent dividend tax credit. It is recommended
26 that this be fully maintained and that further study
27 be devoted to the subject of minimizing double
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1 funds and make recommendations which will encourage
2 increased participation by them.

3 (c) It is recommended that efforts be made
4 to remove some of the competitive disadvantages under
5 which some Canadian firms operate in relation to foreign
6 firms.

7 (d) In regard to the goal of furthering
8 ownership of Canadian equities in Canada, while much
9 has already been done by the companies, the stock
10 exchanges and investment dealers, in close collaboration
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12 improvements are certainly possible and every effort
13 should be made in this direction.

14 (e) While it seems highly desirable for
15 Canadian stock ownership to be broadened, the valuable
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17 development should not be overlooked. It is to be
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APPENDIX K

MUTUAL FUNDS

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Submission by the Investment Dealers'
Association of Canada to the Royal
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APPENDIX - Mutual Funds

A. INTRODUCTION

Brief history of investment companies

1. The forefather of investment companies as such is usually recognized as the Société Générale de Belquique formed in Brussels in 1822 by William I. king of the Netherlands. Initially it was essentially a banking and finance concern but later it developed along holding lines because of its financing operations.

2. The concept of investment trusts was really nurtured in Great Britain. In 1868, the Foreign and Colonial Government Trust was founded for the express purpose of providing "the investor of moderate means the same advantages as the large capitalist, in diminishing the risk in Foreign and Colonial government stocks, by spreading the investment over a number of different stocks". By 1875, eighteen trusts with a paid in capital of over £6.5 million had been formed. During the 1880's the number of trusts more than doubled and the movement was only halted by the Baring Bros. Crisis in 1890.

3. The majority of earlier British trusts either had a termination date or provision in the charter for a gradual redemption of its certificates. A fixed rate -- usually 6 per cent -- was payable on the certificates and earnings in excess of this, after allowance for expenses were used to redeem certificates and/or set up a surplus. It was a normal procedure



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7. The speculative fever of the late 1920's found reflection in the investment companies. Between 1927 and 1930, over 700 investment trusts and investment holding companies, nearly all of which were closed-end, were formed in the United States. All too few of them subscribed to the real tenets of an investment trust and the majority could only be described as proselytes from the conservatism of the true trust. Substantial leverage in the form of debentures and preferred stock was magnified by a combination of pyramiding of one investment company into another with the common shares often having a market price in excess of the break up value.

8. In Canada, investment trusts were also relatively slow in developing. The initial trusts tended to specialize in one industry and in some respects were more holding companies than investment companies. They were practically all closed end management companies.

9. Amongst the first to be formed were Canadian Power and Paper Investments, Ltd. incorporated in 1920 and Power Corporation of Canada, Ltd. formed in 1925. By 1929 there were 49 such investment companies with assets in the order of \$265 million. Some \$230 million of this total was concentrated in nine trusts with Power Corporation of Canada Ltd. being by far the largest with assets of over \$60 million and Consolidated Investment Corporation of Canada second with investments of \$30 million.

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7. The speculative fever of the late 1920's

found reflection in the investment companies. Between 1927 and 1930, over 700 investment trusts and investment holding companies, nearly all of which were closed-and, were formed in the United States. All too few of them subscribed to the real tenets of an investment trust and the majority could only be described as proselytes from the conservatism of the true trust. Substantial leverage in the form of debentures and preferred stock was magnified by a combination of pyramiding of one investment company into another with the common shares often having a market price in excess of the break up value.

8. In Canada, investment trusts were also

relatively slow in developing. The initial trusts tended to specialize in one industry and in some respects were more holding companies than investment companies. They were practically all closed and

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1 end investment companies had leverage to a greater or
2 lesser degree, there was very limited pyramiding when
3 compared with their counterparts in the U.S.A.

4 11. This absence of pyramiding served the
5 Canadian closed-end companies well in helping to reduce
6 the effects of the 1929 Panic. There were reorganizat-
7 ions and consolidations and some liquidations amongst
8 the poorly constituted companies. It must be noted
9 however that generally the major Canadian closed-end
10 trusts of 1929 won through and are in successful
11 operation today.

12 12. Nevertheless, Canadian investors lost
13 heavily on the "investment trusts" and the very term
14 became an anathema to them. It is probable that
15 Canadians were influenced to a degree by the understand-
16 ably bitter attitude of U.S. investors towards trusts.
17 Management as applied to investments was at a discount
18 and the public wanted no part of it.

19 13. Inherently, however, the individual of
20 more modest means still sought ways of investing to
21 provide a combination of diversification over a known
22 list of companies, a redemption or liquidation feature
23 and equally importantly, ways of establishing the proper
24 market value of his commitment.

25 14. The beginning in North America of fixed
26 trusts which in most respects met the new requirement of
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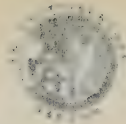
1 there were 52 fixed or semi-fixed trusts in the U.S.A.
2 at the end of 1929 and two years later there were 143.
3 In the two years \$600 million of their certificates
4 were sold.

5 15. The fixed trust movement made limited
6 headway in Canada. There are records for 1931 of four
7 Canadian fixed trusts of which two confined their
8 investments to purely Canadian stocks, while the two
9 others deposited both Canadian and U.S. stocks with
10 their trustees. Several of the larger U.S. fixed
11 trust shares were offered for sale in Canada but the
12 response was not good. Unfortunately there are no
13 accurate records available as to total sales of fixed
14 trust shares in Canada. At the end of 1961 there were
15 only two Canadian fixed trusts reported -- Diversified
16 Income Shares of which there are two series and Trans-
17 Canada Shares with three series of trust shares.

18 B. ADVENT OF MUTUAL FUNDS IN CANADA

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20 movement in investment companies in Canada with the
21 incorporation by Calvin Bullock of Canadian Investment
22 Fund, Ltd. the original mutual investment company of
23 management type in Canada.

24 17. The mutual fund movement developed
25 slowly in Canada. While Canadian Investment Fund, Ltd.
26 had grown steadily since incorporation and was held in
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28 community it was not until 1950 that a new mutual fund
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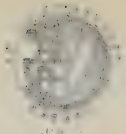
1 been set up primarily for European investment in
2 Canada. Corporate Investors Limited had been organized
3 in 1931 and Commonwealth International Corporation Ltd.
4 in 1933. Both companies are now mutual investment funds
5 in all respects but during their more initial years their
6 operations were essentially those of investment trusts
7 of management type.

8 18. Today there are upwards of 41 mutual funds
9 incorporated in Canada. Of these (a) 24 are essentially
10 Canadian owned and generally come under the definition
11 of Canadian investment companies under the Income Tax
12 Act; (b) 4 are primarily Canadian owned with foreign
13 investments; (c) 3 are owned primarily abroad with
14 investments in Canada, and (d) 10 are non-resident-owned
15 companies registered under the United States Investment
16 Company Act of 1940. A list of the various companies
17 and other details are given in Exhibit A.

18 19. Total Net Assets at market in Canadian
19 dollars at the end of the 1960 (calendar or closest
20 fiscal year) of the various mutual funds incorporate in
21 Canada and investing in Canadian securities was \$900
22 million.

23 20. While an investment company may be defined
24 as an organization that combines the capital of many
25 persons for the purchase of securities, the definition
26 is far from adequate and in particular it makes no
27 reference to professional management.

28 21. The description of purpose given in the
29 prospectus of one of Canada's largest mutual funds
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1 investment company to the investing public. "The
2 fund was formed with a view to providing a convenient
3 medium for diversified investments under careful
4 supervision".

5 22. This concept pertains basically to both
6 closed and open end investment companies. Both types
7 have a definite and useful role in the overall financial
8 community and both have their advantages and dis-
9 advantages from the investors' as well as the capital
10 users' points of view. It is beyond the purpose of this
11 submission to make a comparison of the respective
12 contributions of the two types of the capital markets.
13 Nevertheless, it has to be admitted that the dynamic
14 growth of open-end funds in North America during the past
15 fifteen years when compared with the relatively static
16 position of closed-end investment companies is
17 convincing testimony that collectively mutual funds
18 are developing into an increasingly important sector of
19 the financial markets. See Exhibits D and E.

20 C. A TYPICAL CANADIAN MUTUAL FUND

21 23. While there is a wide variation in
22 objectives, management policies, procedures and operations
23 amongst the individual mutual funds in Canada, they have
24 sufficient features in common to permit the preparation
25 of a description of a prototype or typical Canadian
26 mutual fund. This prototype, in addition to being a
27 corporate picture of a mutual fund, serves as a yardstick
28 for measuring deviations from the average practice
29 employed by funds to achieve their individual objectives.

30 24. The typical Canadian fund would have a



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1 simple capital structure consisting of a large number
2 of redeemable special shares and a very small number
3 of deferred shares which latter would be held by the
4 management group. Both classes of stock have full voting
5 rights. The holders of the Special Shares would have
6 the right at their option to present their shares to
7 the company for redemption at the net asset value,
8 whereas this privilege is not available to the deferred
9 shareholders. In all other respects the stocks rank
10 pari passu.

11 25. The company would be prohibited from
12 borrowing money, buying securities on margin or selling
13 short. Its investments would consist of possibly 70
14 different common stocks of prominent Canadian companies
15 and some common stocks of a few large U.S. corporations
16 -- 15 per cent of the investments would be in preferred
17 stocks and corporate bonds, a portion of which would have
18 a conversion or similar feature and depending upon the
19 state of the markets a larger or smaller amount of
20 Government of Canada bonds.

21 26. The by-laws of the fund would prohibit
22 it from placing more than 5 per cent of its assets in
23 the securities of any one corporate issuer and would
24 also prohibit the holding of more than 5 per cent of the
25 voting securities of any one corporate issuer.

26 27. Dividends would be paid quarterly out of
27 the income received by the fund on the securities held
28 after allowance for corporate and other expenses. It is
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1 no cost, in the Special Shares of the fund. Shareholders
2 would also receive, quarterly, a list of securities held
3 by the fund, together with information as to changes made
4 during the quarter.

5 28. The fund would be operated by an invest-
6 ment management organization that in addition to
7 providing office accommodation, administrative and
8 clerical services would supply the complicated research
9 work necessary in the professional management of the
10 company's portfolio. Such management would be subject
11 to the control of the nine man board of directors, four
12 of which might well be connected with the management
13 organization.

14 29. The management fee would be one half of
15 one per cent a year of the average daily net asset
16 value of the fund, calculated and payable on a quarterly
17 basis. Other expenses of the fund would include
18 security transaction commission, custodian, legal,
19 dividend paying and auditing fees together with the
20 usual costs of shareholder reports, annual meetings,
21 etc.

22 30. There would be adequate provision in the
23 fund's charter to ensure "arms length dealing" with the
24 investment management and members of the board of
25 directors on all transactions other than those conducted
26 in securities listed on a stock exchange where regular
27 commissions or brokerage are charged.

28 31. The underwriter of the funds Special
29 Shares would be the investment management organization.
30 It would purchase the shares at their net asset value



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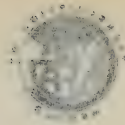
1 and sell them to investment dealers who in turn would
2 sell them to their clients. The retail price would be
3 the net asset value which would be calculated daily,
4 plus a loading charge of 8 per cent of the offering
5 price. The fund also has a sliding scale of loading
6 charges whereby the load is reduced to 5 per cent with
7 the purchase of \$50,000 and to lower rates as the
8 total purchases increase.

9 32. The bulk of the loading charge would be
10 paid to the investment dealer who has undertaken to sell
11 the special shares only at the net asset value plus
12 the specified loading charge. The balance of the
13 loading charge is retained by the underwriter to defray
14 the expenses of prospectuses and other sales literature,
15 advertising, etc. This charge is commented upon in
16 more detail in paragraphs 48 to 55 inclusive.

17 33. The investment management organization,
18 which is also the underwriter, has followed the practice
19 of managements of several other larger Canadian funds
20 of having its own sales force to sell the Special
21 Shares direct to the public in addition to selling them
22 to investment dealers.

23 D. CENSUS OF CANADIAN MUTUAL FUNDS

24 34. For the purposes of this study 41 mutual
25 funds incorporated in Canada have been examined. There
26 are a few additional funds in Canada but these are all
27 small and it is questionable if their combined net
28 assets at market exceed \$500,000. Also excluded
29 from this count are mutual funds that invest only in
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Department of Finance
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1 of this (as shown in Exhibit A) is All-Canadian
2 Compound Fund that purchases only the shares of All-
3 Canadian Dividend Fund.

4 35. Of the 24 Canadian owned mutual funds
5 studied, 12 are classified as balanced funds, 7 are
6 essentially common stock funds and 5 are considered
7 specialty funds. The term "balanced fund" indicates
8 that the objectives of the fund include both a regular
9 reasonable income and capital appreciation. The common
10 stock fund usually has capital growth as its major
11 objective and might well be called a growth fund.

12 36. The specialty funds are those that have
13 some feature that separates them from the other two
14 groups. Of the five specialty funds, two concentrate
15 their investments in Canadian oil and gas and related
16 companies; one is a mutual bond fund, one purchases
17 only the shares of three other designated mutual funds
18 and one has a leverage feature whereby under specified
19 conditions it is permitted to borrow money. This
20 feature has not been used during the past four years.

21 37. The second group of mutual funds, shown
22 in Exhibit A, are funds incorporated in Canada with
23 their principal assets being Canadian securities but
24 whose shares are distributed largely outside of Canada.
25 It is not known whether sufficient amounts of their
26 shares are held externally for them to qualify as Non-
27 Resident-Owned Investment Corporations. All three
28 unfds are classified as the balanced type.

29 38. The third group of mutual funds are those
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1 Corporations which are registered under the United
2 States Investment Act of 1940. There are ten of these.
3 None of them pay dividends and all reinvest their
4 income. Accordingly, they should be classified as
5 growth funds.

6 39. The fourth group are Canadian incorporated
7 mutual funds owned by Canadian investors but with their
8 investments being made in the United States and Europe.
9 There are four of these. All of them are classified as
10 growth funds.

11 E. TAXATION

12 40. The Canadian Government has recognized
13 the need of investors who wish to have the protection
14 afforded by a diversified investment portfolio but who
15 at the same time may not have the means, time or
16 facilities to create and operate efficiently such a
17 portfolio, but granting tax concessions to those which
18 wish to pool their resources in an investment company
19 that complies with conditions specified in the Income
20 Tax Act.

21 41. Those sections of the Income Tax Act
22 pertaining to Investment Companies (Section 69) and
23 to Non-Resident-Owned Investment Corporations (Section
24 70) are given in Exhibit B.

25 42. Investment companies (domestic) pay a tax
26 of 21 per cent of their taxable income providing they
27 meet certain requirements and at the same time because
28 the investment company is not exempt from tax, the
29 Canadian shareholders of such a company are not
30 precluded from claiming the 20 per cent dividend credit



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1 under Section 38 of the Act.

2 43. To qualify as an "investment company"
3 the following conditions must be met by the company:

4 (a) At least 80 per cent of its
5 property, through the year, must be
6 securities or cash.

7 (b) At least 95 per cent of its income
8 must be derived from the investments
9 mentioned in A.

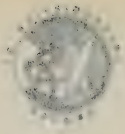
10 (c) Not less than 85 per cent of its
11 gross revenue is from sources in
12 Canada. Investment companies with
13 less than 85 per cent in the 1962 tax
14 year but 75 per cent or more are given
15 to the 1963 tax year to meet this
16 requirement.

17 (d) Not more than 25 per cent of its
18 gross revenue for the year was from
19 interest. Companies with a higher
20 gross from interest are given until
21 1963 to comply with this requirement.

22 (e) Other than Government, Provincial
23 and Municipal securities not more than
24 10 per cent of its assets must be in the
25 securities of one corporation.

26 (f) There must be a minimum of 50
27 shareholders, none of whom hold more
28 than 25 per cent of the shares of the
29 investment company.

30 (g) The investment company must distribute



Income Tax Act
Section 38

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(a) At least 80 per cent of the property, through the year, must be securities or cash.

(b) At least 95 per cent of its income must be derived from the investments mentioned in A.

(c) Not less than 85 per cent of its gross revenue is from sources in Canada, less than 35 per cent in the 1963 tax year but 75 per cent or more are given to the 1963 tax year to meet this

(d) Not more than 25 per cent of its gross revenue for the year was from interest. Companies with a higher gross from interest are given until 1963 to comply with this requirement.
(e) Other than Government, Provincial and Municipal securities not more than 10 per cent of its assets must be in the securities of one corporation.

(f) There must be a minimum of 50 shareholders, none of whom hold more than 25 per cent of the shares of the

(g) The investment company must distribute



1 to its shareholders before the end
2 of the taxation year at least 85 per
3 cent of the taxable income after
4 allowing for the tax paid. Shareholders
5 are entitled to the usual depletion
6 allowances. Dividends paid to non-
7 resident shareholders are subject to
8 the 15 per cent withholding tax.

9 44. Non-Resident Owned Investment Corporations

10 are also not subject to the usual rates of corporation
11 income tax providing such an investment company elects to
12 be so classified and meets the necessary qualifications.
13 This special class of taxpayer was originally established
14 to attract foreign capital to Canada.

15 45. Providing that the company qualified as a
16 non-resident-owned investment corporation under Section
17 70 of the Income Tax Act it is subject to tax of 15 per
18 cent on the taxable income as determined in the manner
19 prescribed in the Act.

20 46. Briefly the major requirements for a
21 company to qualify as a N.R.O. investment corporation
22 are:

23 (a) At least 95 per cent of the aggregate
24 value of the issued shares and 100 per cent
25 of its bond or other indebtedness must be
26 beneficially owned by non-resident
27 persons.

28 (b) The second general qualification
29 relates to the source of income which must
30 be limited to that from:



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non-resident-owned investment corporation under Section
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cent on the taxable income as determined in the manner
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company to qualify as a N.R.O. investment corporation

(a) At least 25 per cent of the aggregate
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(b) The second general qualification
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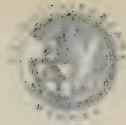
- i. ownership or trading securities,
bills, notes or other property.
- ii. lending money
- iii. rents, hire or chattels, annuities,
royalties, etc.
- iv. estates or trusts.

(c) The principal business of the N.R.O. corporation shall not be the making of loans or the trading or dealing in mortgages, hypothecates, bills, notes, etc. Not more than 10 per cent of the company's gross revenues may be derived from rents, hire of chattels or charter party fees.

(d) While the company may receive its income from almost any type of property as mentioned in (b) and (c) it must derive no revenue from business activities such as purchasing, processing, merchandising, manufacturing or similar activities. The receipt of any income that does not qualify disqualifies the company in toto.

F. SELLING COSTS

48. The majority of mutual funds charge the purchase a fee, or selling charge which is over and above the net asset value of the shares. This fee -- commonly called the "loading" -- is, in Canada, usually between 8 per cent and 9 per cent of the offering price of the shares. Normally the loading is scaled down as



i. ownership on trading securities,

ii. interest on other securities,

iii. lending money

iv. rents, hire on chattels, annuities,

royalties, etc.

v. estates or trusts.

(c) The principal business of the N.R.C.

corporation shall not be the making of

loans or the trading or dealing in

mortgages, hypothecates, bills, notes,

etc. Not more than 10 per cent of the

company's gross revenues may be derived

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above the net asset value of the shares. This fee --

commonly called the "loading" -- is, in Canada, usually

between 8 per cent and 9 per cent of the offering price

of the shares. Normally the loading is scaled down as



1 the amount purchased increases after a certain minimum
2 is passed.

3 49. A few mutual funds in Canada have a low
4 loading charge or no charge at all at the time of
5 purchase but levy a small redemption fee when the shares
6 are presented for redemption.

7 50. It is often claimed by superficial
8 observers that in relation to normal commission charges
9 on the Toronto or Montreal Stock Exchanges the "loading
10 charges" are exorbitant. Such a comparison is both
11 fallacious and misleading as the two things compared are
12 entirely dissimilar and several important factors are
13 ignored.

14 51. A share of a mutual fund is not an
15 ordinary "security". It not only represents pro-rata
16 ownership in the net assets of the fund but it is in
17 effect a service contract entitling the holder to the
18 benefits of constant professional management at very low
19 cost of his interest in a highly diversified and large
20 portfolio.

21 52. Mutual funds shares in common with goods,
22 services and insurance have to be "sold" and the real
23 benefits of diversification and professional management
24 can only be obtained if a sufficient number of shares
25 are sold to provide a large pool of capital. Those
26 engaged in the creation of such a pool are entitled to
27 compensation for their efforts.

28 53. It should also be noted that the loading
29 on mutual fund shares covers sale as well as purchase
30 as usually there is no charge for redemption. Stock



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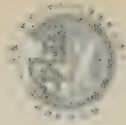
1 exchange commissions and taxes (where applicable) are
2 charged on sales as well as on purchases.

3 54. Another aspect that should be considered
4 when examining the offering price and redemption price
5 of mutual fund shares is the spread between the bid
6 and asked prices that normally prevail both on listed
7 stocks and those traded over-the-counter. Set out in
8 Exhibit C is an analysis of the difference between the
9 total cost of the purchase of the first fifteen common
10 stocks on the Montreal Stock Exchange at the closing
11 asked prices and the proceeds when they are sold at
12 the closing bid prices for four separate days. The
13 percentage spread between the Total Cost and the Net
14 Proceeds ranged between 6.84 per cent on July 21, 1957
15 and 4.45 per cent on May 31, 1960.

16 55. The calculations set out in Exhibit C
17 cover the purchase and sale of more than "board lots"
18 of each stock. If, however, the individual sought some
19 diversification by spreading a modest amount of money
20 over a number of stocks he is likely to encounter minimum
21 commissions and when buying or selling small or odd
22 lots of stock a wider than normal spread between the bid
23 and asked prices. Accordingly it is likely that the
24 percentage spread would be higher than the examples given
25 in Exhibit C.

26 G. MARKETING OF MUTUAL FUNDS

27 56. Shares of mutual funds in Canada are, for
28 the most part, sold in one or a combination of three
29 ways. The underwriter, which is usually the fund
30 manager, purchases the shares from the mutual fund and



exchange commissions and taxes (where applicable) are charged on sales as well as on purchases.

54. Another aspect that should be considered when examining the offering price and redemption price of mutual fund shares is the spread between the bid and asked prices that normally prevail both on listed stocks and those traded over-the-counter. Set out in Exhibit C is an analysis of the difference between the total cost of the purchase of the first fifteen common stocks on the Montreal Stock Exchange at the closing asked prices and the proceeds when they are sold at the closing bid prices for four separate days. The percentage spread between the Total Cost and the Net Proceeds ranged between 6.84 per cent on July 21, 1957 and 4.45 per cent on May 31, 1960.

55. The calculations set out in Exhibit C cover the purchase and sale of more than "board lots" of each stock. It, however, the individual sought some diversification by spreading a modest amount of money over a number of stocks he is likely to encounter minimum commissions and when buying or selling small or odd lots of stock a wider than normal spread between the bid and asked prices. Accordingly it is likely that the percentage spread would be higher than the examples given in Exhibit C.

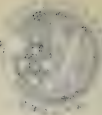
G. MARKETING OF MUTUAL FUNDS

56. Shares of mutual funds in Canada are, for the most part, sold in one or a combination of three ways. The underwriter, which is usually the fund manager, purchases the shares from the mutual fund and



1 then sells them to investment dealers who, in turn,
2 offer them to the investing public at the net offering
3 price, which includes the loading charge. The
4 investment manager, or underwriter, may also, in
5 addition to selling to investment dealers, have his
6 own sales force which is engaged in distribution of the
7 shares to the investing public at exactly the same price
8 as they are available from investment dealers. A third
9 method is for a separate organization (with its own
10 sales force) that is entirely independent of either the
11 underwriter or investment dealers to purchase shares
12 under an arrangement from the underwriter and offer
13 them for sale under some form of a contractual plan
14 (described in paragraphs 61 to 65) which may well also
15 embody term insurance.

16 57. In addition to mutual fund sales made
17 as individual transactions which are conducted in the
18 same manner pertaining to other securities, mutual
19 fund sales are also made in increasing amounts under
20 where are known as Accumulation or Regular Purchase
21 Plans under which the investor is able to take advantage
22 of "dollar cost averaging". By this is meant that the
23 individual invests a stated amount of money at regular
24 intervals in the shares of a mutual fund. His money
25 will buy more shares when prices are down and less
26 shares when prices are high. It is arithmetically
27 proveable that at the completion of a market cycle --
28 namely when a recognized stock exchange index of common
29 stocks returns, in due course, to the level existing at
30 the time of the investor's first purchase -- it will be



...the ...

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provided that at the completion of a market cycle --

namely when a recognized stock exchange index of common

stocks returns, in due course, to the level existing at

the time of the investor's first purchase -- it will be



1 found that the market value of the combined holdings
2 exceeds that paid for such holdings, entirely apart
3 from any dividends that may have been received in the
4 interim. It must be assumed that the price of the
5 mutual fund shares will move in reasonably close
6 conformity with the stock exchange index that is being
7 used as a yardstick. In most cases, however, it will
8 be found that, because of the professional management,
9 the mutual fund shares will have done better than the
10 averages.

11 Accumulation or Regular Purchase Plans.

12 58. Generally speaking these plans are based
13 on regular contributions on a monthly, bi-monthly or
14 quarterly basis. Dividends may or may not, as decided
15 by the investor, be reinvested, usually at no cost to
16 the investor.

17 59. (i) Voluntary Plans - These provide a
18 systematic method whereby the holder elects to make
19 periodic (usually regular) purchases of a mutual fund.
20 The bookkeeping details, reinvestment of dividends, T-4
21 slips, quarterly and annual reports, etc., are usually
22 handled by the underwriter of the fund or by an
23 independent trust company whose services are employed
24 by the fund management.

25 60. The holder has the right to terminate
26 or liquidate his plan at any time without penalty. If
27 he decides to present his shares to the fund for
28 redemption, he will receive the net asset value
29 prevailing at that time.

30 61. (ii) Contractual Plan - In the past five

prevailing at that time.
redemption, he will receive the net asset value
he decides to present his shares to the fund for
or liquidate his plan at any time without penalty. If

60. The holder has the right to terminate
by the fund management.

Interim: After each year, the fund will
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1 years the number of contractual plans being sold have
2 increased rapidly in Canada. This may be attributed
3 mainly to the type of distribution being carried out
4 by the direct sales forces of many of the funds
5 underwriters' and also independent organizations that
6 are engaged in selling several variations of the
7 contractual plan.

8 62. Under the contractual plan, the holder
9 agrees to make contributions for the purchase of a
10 mutual fund shares of stipulated amounts at regular
11 specified intervals for a pre-determined number of
12 years, usually ten, fifteen, or twenty years. The
13 terms of the contract carry certain penalties to the
14 holder in the event that he is unable to continue his
15 payments until the maturity date of the plan.

16 63. Contractual plans for some mutual funds
17 have what is known as a "front-end load". Under such
18 a plan a material part of the total load which would be
19 paid to carry the plan to completion is concentrated
20 in the first two or three years of the plan. The result
21 is that if the investor is forced to terminate the plan
22 in the earlier years of its life, he will only recover
23 part of the total amount he has paid in. Certain
24 provincial regulatory bodies have objected to this
25 "front-end loan" practice and at least one fund sales
26 organization was required to modify its contractual plan
27 and lower the "front-end load" on sales made in those
28 provinces. Later, the sales organization voluntarily
29 introduced the modifications for sales in all provinces.
30 It should be noted that the loading charge per share of



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1 the fund is unchanged from that pertaining to regular
2 sales but a major portion of the total is collected
3 early in the contract in anticipation of subsequent
4 share purchases.

5 64. In effect, the contractual plan employs
6 the principle of compulsory savings which to some
7 investors may well be beneficial. On the other hand,
8 it cannot be overlooked that if for some involuntary
9 reason the purchaser has to terminate the plan in the
10 earlier years of its life, he could suffer a material
11 loss of capital without the interim compensating
12 feature which applies to insurance.

13 65. Many contractual plans offer a form of
14 reducing term insurance at additional cost to the
15 holder. In most instances the combination of the
16 insurance and the contribution will provide the
17 beneficiaries with the face amount of the plan in the
18 event of the holders death.

19 66. By far the greater majority of regular
20 purchase plans are directed to small investors -- those
21 people are are able to save and invest from \$15 to
22 \$100.00 per month. Most mutual funds, after an initial
23 moderate deposit, carry a low minimum contribution under
24 the voluntary plan. This in many cases is as low as
25 \$100 per year. Contractual plans may have a minimum
26 deposit as low as \$10 a month and often require no
27 initial deposit of larger than this amount.

28 H. RETIREMENT SAVINGS PLANS

29 67. In 1957, the Government of Canada amended
30 the Income Tax Act to permit any Canadian whether



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1. INVESTMENT SAVINGS PLANS

67. In 1957, the Government of Canada amended the Income Tax Act to permit any Canadian whether



1 employee or employer to make certain tax exempt
2 contributions to a Registered Pension Plan which would
3 provide funds for retirement years.

4 68. Under the terms of the Plan, a self-
5 employed person may contribute each year up to 10 per
6 cent of annual earned income with a maximum of \$2,500
7 and such a contribution is deductible from taxable
8 income. For those who are members of a group plan, to
9 which their employer also contributes, the maximum
10 deduction is \$1,500. When contributions to such group
11 plans are less than the maximum tax deductions
12 permitted, the individual taxpayer may establish a
13 supplementary individual registered pension plan so as
14 to obtain the full benefit of the allowable deduction.

15 69. The plan-holder has the option of
16 converting the assets of the Plan to an annuity at
17 any time prior to his or her 71st birthday, at which
18 time the assets will automatically be converted under
19 the terms of the Plan.

20 70. Mutual funds qualify as an investment
21 medium for Registered Retirement Savings Plans. As a
22 result of the introduction of Registered Pension Plans
23 in 1957, a new outlet for fund sales has developed.

24 I. WITHDRAWAL PLANS

25 71. A number of mutual funds provide what
26 amounts to a bookkeeping service whereby a shareholder
27 who had acquired a block of shares of the fund (either
28 as a lump purchase or by gradual accumulation) may elect
29 to liquidate a portion of his holdings at stipulated
30

employee or employer to make certain tax exempt contributions to a Registered Pension Plan which would provide funds for retirement years.

68. Under the terms of the plan, a self-employed person may contribute each year up to 10 per cent of annual earned income with a maximum of \$2,500 and such a contribution is deductible from taxable income. For those who are members of a group plan, to which their employer also contributes, the maximum deduction is \$1,500. When contributions to such group

plans are less than the maximum tax deductions permitted, the individual taxpayer may establish a supplementary individual registered pension plan so as to obtain the full benefit of the allowable deduction.

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1 regular intervals -- usually monthly but in some cases
2 quarterly or annually.

3 72. This service is not in any way the
4 payment of an annuity but constitutes simply a
5 convenient method for a shareholder to gradually withdraw
6 invested capital for other purposes -- usually to
7 supplement other sources of revenue. It has the
8 advantage from the shareholders point of view of economy.
9 In most cases the dividend being received on the shares
10 still held are reinvested at no cost and there is no
11 charge for the liquidation of shares.

12 73. The usual options available to the
13 shareholder are:

14 (i) The liquidation of a sufficient
15 number of shares on a given day each
16 month to provide the shareholder with
17 a stated number of dollars.

18 (ii) The liquidation of a stated number
19 of shares on a given day each month
20 until all the shares have been
21 redeemed. In this case, the number
22 of dollars received will vary with the
23 price of the stock.

24 74. Most of the funds providing this service
25 require a minimum purchase or accumulation of \$6,000
26 in its shares at the commencement of the service and
27 that, under option one, not more than 10 per cent of the
28 initial invested capital may be redeemed each year.

29 75. With this type of service the shareholder
30 has no guarantee that his original invested capital will

... usually ...
... usually ...

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of dollars received will vary with the
price of the stock.

74. Most of the funds providing this service

require a minimum purchase or accumulation of \$5,000
in the shares at the commencement of the service and
that, under option one, not more than 10 per cent of the
initial invested capital may be redeemed each year.

75. With this type of service the shareholder

has no guarantee that his original invested capital will



1 not be exhausted. The funds offering this service
2 are careful in emphasizing the absence of the guarantee.
3 It has to be admitted, however, that, for the
4 individual who is experienced investment-wise, the
5 service can appear complicated and unless it is
6 explained to the shareholder by a highly experienced
7 salesman, misunderstandings could occur. Market
8 experience over the past eleven years has been
9 favourable to most of these services (see Exhibit F).
10 There can, however, be no assurance or guarantee that
11 this experience will repeat itself in the future.

12 J. CANADIAN MUTUAL FUND EXPERIENCE

13 76. A study of mutual funds in Canada is
14 rendered more difficult because of the absence of a
15 central supervisory body of a similar nature to the
16 U.S. Securities and Exchange Commission to which
17 American investment companies must report. The student
18 of the American scene is further helped by the presence
19 of the National Association of Investment Companies --
20 a non-profit organization maintained by the great maj-
21 ority of important registered investment companies in
22 the United States.

23 77. In the United States the two first
24 mutual funds -- Massachusetts Investors Trust and State
25 Street Investment Corporation -- were formed in 1924.
26 In Canada the first fund, Canadian Investment Fund,
27 Ltd., was formed late in 1932. It was not until the
28 1950's that it was joined by other mutual funds of
29 substance. Of the fifteen domestic mutual funds with
30 net assets (at market) at the end of 1960 of \$1 million



not be overstated. The funds offering this service are careful in emphasizing the absence of the guarantee. It has to be admitted, however, that, for the individual who is experienced investment-wise, the service can appear complicated and unless it is explained to the shareholder by a highly experienced salesman, misunderstandings could occur. Market experience over the past eleven years has been favourable to most of these services (see Exhibit F). There can, however, be no assurance or guarantee that this experience will repeat itself in the future.

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77. In the United States the two first mutual funds -- Massachusetts Investors Trust and State Street Investment Corporation -- were formed in 1924. In Canada the first fund, Canadian Investment Fund, Ltd., was formed late in 1932. It was not until the 1950's that it was joined by other mutual funds of substance. Of the fifteen domestic mutual funds with net assets (at market) at the end of 1960 of \$1 million



1 or more each, fourteen were incorporated in or started
2 their period of active growth during the 1950 decade.
3 Accordingly, it has been necessary to refer from time
4 to time to the experience in the United States to
5 obtain longer term mass indications of trends and
6 responses to developments.

7 78. Just as the investment trust of old
8 was a British development designed "to provide the
9 investor of modest means the same advantages as the
10 large capitalistby spreading the investment over
11 a number of government loans" so it must be said that
12 the open-end investment company or mutual fund is
13 a distinctly United States development that in addition
14 to permitting "the investor of modest means" to obtain
15 the advantages of diversification, enables him to
16 become a true participant or shareholder in actual
17 industry under skilled professional investment management.

18 79. The mutual fund was slow to develop
19 in the United States and still slower in Canada.
20 According to the SEC Report (Securities and Exchange
21 Commission. Investment Trusts and Investment Companies
22Washington, D.C., Government Printing Office 1939-
23 42.) as at December 31, 1929, there were 675 investment
24 companies of all types in the United States with total
25 assets of \$7,157 million. Of these 19 only were open-
26 end companies with assets of a mere \$140 million.

27 80. The year 1932 is generally regarded by
28 historians as the true beginning of the mutual fund in
29 the United States. During and after that year, to date,
30 nearly all newly organized investment companies were of



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1 the mutual fund type. In Canada, with the exception
2 of the previously mentioned Canadian Investment Fund
3 Ltd. and a few small Fixed Trusts, there were
4 practically no new investment companies organized until
5 after the War. It was not until the "50's, however,
6 that the mutual funds became popular with the Canadian
7 investing public.

8 81. Set out in Exhibit D is a record of the
9 growth of the five largest of the Canadian owned,
10 domestic mutual funds from the years 1950 to 1961.
11 These five companies at the end of 1960 represented
12 approximately 82 per cent of the total net assets (at
13 market) of all the 24 Canadian mutual funds and
14 accordingly could be considered representative in the
15 absence of detailed statistics of other funds in the
16 earlier years. The consistent growth over the years
17 under review of combined net assets of over 1000 per
18 cent is considered impressive and indicative of the
19 acceptance of mutual funds as an investment instrument.

20 82. Exhibit E shows the growth of United
21 States mutual funds during the years 1940 to 1960 when
22 Total Net Assets increased from \$448 million to \$17
23 billion. The increase from 1950 to 1960 was approximately
24 \$14.5 billion or roughly 500 per cent.

25 K. RUN ON THE BANK

26 83. Apprehension has been expressed from time
27 to time that during periods of recession, international
28 crises and sharp or extensive declines on the market
29 that many mutual fund shareholders would redeem their
30 shares, thus forcing the funds to sell heavily on

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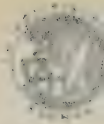


1 balance. This in turn would tend to depress stock
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3 84. Many careful studies of the history of
4 the mutual funds in the United States have been made by
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12 in the United States investment industries, states:

13 "The NIAC has figures from its
14 mutual fund members (representing
15 74 per cent of the assets of its
16 mutual fund members) showing that
17 during the 18 per cent stock market
18 decline from May to October in 1946,
19 the public purchased shares from such
20 funds valued at \$98 million and asked
21 the funds to redeem \$39 million worth
22 of their shares. Meanwhile the
23 funds' purchases of portfolio
24 securities were \$117 million and their
25 sales of portfolio securities \$72
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1 30, 1950, investors purchased \$9
2 of shares and redeemed \$8 million.
3 Meanwhile the mutual funds themselves
4 purchased \$14 million of portfolio
5 securities and sold only \$6 million.
6 Then, during the week ending September
7 30, 1955, when President Eisenhower
8 was first taken seriously ill and the
9 market declined over 4 per cent 82
10 per cent of the NAIC mutual fund
11 members (by assets) reported that
12 investors purchased \$22 million and
13 redeemed \$10 million, and the funds
14 themselves purchased \$16 million
15 portfolio securities and sold \$13
16 million. Similarly in the market
17 break from October 1 to 21 in 1957 a
18 survey of mutual funds, the assets
19 of which represented 79 per cent of
20 the NAIC memberships' showed that
21 the ratio of the funds' sales of
22 their shares to repurchase of such
23 shares was \$47 million to \$16 million
24 or almost 3 to 1, while the companies
25 purchased \$81 million of portfolio
26 securities and sold only \$32 million."
27 (The Story of Investment Companies by
28 Hugh Bullock, Columbia University Press,
29 New York, 1959 - pages 162-3).
30 86. The 1929-32 Crisis was beyond question the



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(The Story of Investment Companies by

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1 severest test experienced by mutual funds. It should
2 also be noted that this test came at a time when the
3 mutual funds movement in the United States was of only
4 relatively modest proportions. The SEC Report states:

5 "At the end of September 1929

6 Massachusetts Investors Trust had
7 298,687 shares outstanding. From
8 that date until December 31, 1932, it
9 was called upon to repurchase 235,016
10 of its outstanding shares. Thus, if
11 no new sales of shares had been
12 effected, the amount of assets of
13 the company would have been reduced
14 by almost 80 per cent by virtue of
15 these redemptions alone. However,
16 at the close of 1932 this company
17 had outstanding 951,752 shares."

18 (Report of the Securities and Exchange
19 Commission - Investment Trusts and
20 Investment Companies 1939 - 42.)

21 87. No such wealth of statistics is available
22 for Canada. It is felt, however, that the experience
23 of Canadian Investment Fund, Ltd. from 1933 to 1961
24 (as shown in Exhibit G) provides much more than a
25 hypothetical answer as to what would have occurred if
26 the mutual fund business in Canada had been much larger.

27 88. During the 29 years of its existence,
28 Canadian Investment Fund, Ltd. had net redemptions in
29 only four years. It may be of some significance that
30 three of these years (1945, 1946 and 1961) were in



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1 periods of high and rising market levels and not low
2 markets. The vice-president, and treasurer of the Fund
3 advises that in 1940, the redemptions were from non-
4 residents of Canada and that on balance Canadians were
5 buyers. It is possible that expropriation of dollar
6 securities of the British Government during 1940 may
7 have contributed to the redemptions by non-residents.

8 89. The experience of Investors Mutual of
9 Canada Ltd. from 1950 to 1961 is given in Exhibit H
10 while the overall picture of the five largest balanced
11 funds for the same period is given in Exhibit D.
12 Consistent growth during each of the 11 years is to be
13 noted.

14 90. It is difficult to assess the importance
15 of the trend of the Canadian incorporated N.R.O. mutual
16 funds registered in the United States as shown in
17 Exhibit J. While the combined figures show a rise in
18 the number of shares outstanding and in net value of
19 assets for the years 1955 to 1958 and a decline during
20 the next two years, the trends of some of the individual
21 funds do not always conform with the overall pattern.
22 The decline that occurred in 1959 and 1960 are of
23 appreciable, but not damaging proportions and may well
24 be no more than a reflection of a tendency to be noted
25 from time to time in many sections of the security
26 markets of investors to repatriate part of their
27 foreign commitments during periods of indefinite trends.
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29 U.S. investors felt that there were more attractive
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1 91. Information as to how mutual funds that
2 have specialized in some particular industry or group
3 of industries such as atomic energy, electronics, or
4 oil and gas have fared during different phases of the
5 market is not available. In Canada, there are only
6 two funds that have specialized in a particular
7 industry. Both of these are relatively recent
8 incorporations. First Oil and Gas Fund was formed in
9 1959 and while Growth Oil and Gas Investment Fund was
10 formed in 1952, its expansion has been quite modest.

11 92. It is difficult to establish any
12 definite relationship between the size of the Canadian
13 securities market as a whole and the participation of
14 the mutual funds in them. The net asset value (at
15 market) of all mutual funds in Canada at the end of
16 1960 was approximately \$900 million. Because the
17 assets of the Non-Resident-Owned mutual funds are almost
18 entirely Canadian securities their net asset values at
19 market of \$337 million have been included in the \$900
20 million figure.

21 93. Complete figures are not yet available
22 but it is estimated that the net asset value (at market)
23 of all mutual funds in Canada at the end of 1961 was
24 somewhat in excess of \$1 billion.

25 94. At the end of 1961 the quoted market
26 value of all stocks listed on the Toronto Stock Exchange
27 was \$61 billion while the market value of listings on
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1 amount of duplication arising from inter-listings
2 the quoted market value of stocks on the Toronto,
3 Montreal and Canadian Stock Exchanges is estimated at
4 under \$62 billion. This figure may be further refined
5 by elimination of the market value of \$34 3/4 billion of
6 the 21 foreign companies (mainly U.S. concerns) whose
7 shares are listed in Canada and other countries, thus
8 leaving a market value of listed Canadian stocks at
9 the end of 1961 in the order of \$30 billion. Of this
10 sum preferred stocks had a market value of approximately
11 \$1 billion.

12 95. This \$30 billion market of listed
13 Canadian stocks include shares of all grades across the
14 entire investment spectrum from the most speculative to
15 the most conservative. While there is no real basis
16 for an accurate estimate, it is probably that some two-
17 thirds of the value of the listed Canadian stocks would
18 be of an investment grade that might make them potential
19 candidates for inclusion in a mutual fund portfolio of
20 today.

1 L. CONCLUSION

2 96. The gradual and accelerating interest in
3 equities throughout the Free World during the past
4 sixty to one hundred years may be regarded as the natural
5 evolution of man's desire to share or participate in the
6 growing economy of the nations and thus increase his
7 stature. It may also be said that the right as an
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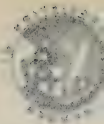
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97. The Radcliffe Committee in its detailed



report upon the working of the British monetary system states:

"574. The third factor tending to drag up the bond yield may be the most fundamental of all, but fortunately it need not be dangerous. This is the shift of investors, notably insurance companies and pension funds, from bonds to equities. This shift is partly due, no doubt, to fears of inflation;

but partly also to the development of institutional facilities for investing with reasonable safety in equities, to the influence of financial journalism, and most of all, perhaps to the belief that a well-spread portfolio of equities gives the investor the chance to share in the benefits of economic growth. Experience seems to have borne out this expectation (though not as dramatically as is sometimes suggested) and, now that development of financial institutions is freer, it is reasonable to expect that the swing will continue." (Para. 574 - page 212 - Report of the Committee on the Working of the Monetary System - Chairman the Rt. Hon. the Lord Radcliffe, G.B.E., Her Majesty's Stationery Office 1959, Cmnd. 827.)



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Mr. J. H. Macdonald

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1 98. Recognition of the part that equities
2 play in investment is given by the Government in the
3 authorization of Registered Pension Funds to include
4 common stocks in their portfolios and by permitting
5 the acquisition of maximum stipulated amounts of
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7 also extended to self-employed professional or business
8 men, the right to participate in equities in the creation
9 of a pension estate by allowing him to deposit shares of
10 recognized mutual funds as contributions to his
11 Registered Pension Fund. No other direct corporation
12 equities may be deposited. The self-employed person
13 is thereby accorded the same privilege as if he were a
14 member of a corporation employee pension fund.

15 99. Investment companies are the only
16 financial institutions through which investors of
17 moderate means can share directly in the risks and
18 rewards of equity investment under professional manage-
19 ment conservatively and with the protection of broad
20 diversification and continued supervision. The pooled
21 funds now being made available to investors by certain
22 of the Canadian trust companies may well be included in
23 the investment company classification.

24 100. It is not desired to discuss or make a
25 comparison of the relative merits of the closed-end
26 and open-end investment companies. Each has a place
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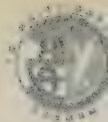


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4 101. The dynamic growth of mutual funds in
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6 ors at large are being offered or sold a security that
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8 102. The features of redemption of shares at
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12 The other aspect is that, in common with most forms of
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14 provide a service which the investment dealer or a
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16 the same time the service fills a need not before
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22 103. There is a sufficient allowance in the
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1 104. The combined net asset value of all
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3 108. For the individual mutual fund share-
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12 109. From the Canadian mutual fund point of
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15 quality in some industries such as electronics and
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22 foreign corporations operating in Canada are making
23 their securities available to the Canadian investing
24 public. This, however, cannot be regarded as the
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1 in its view and if it is to exercise its policies to
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5 111. While the present requirement under the
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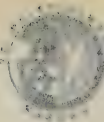
1 that in the absence of special regulatory legislation
2 pertaining to investment companies at either or both
3 federal or provincial levels the various provincial
4 Securities Commissions may be faced with some
5 difficulties in protecting the investing public.

6 115. It is beyond the scope of this sub-
7 mission to discuss investment company regulations in
8 detail. It is suggested, however, that the Commission
9 satisfy itself that present provincial legislation
10 provides adequate safeguards for the protection of
11 shareholders of both open and closed end investment
12 trusts.

13 116. As the sale of few if any mutual funds
14 will be limited to one province it is essential that
15 there is uniformity of legislation and its administration
16 in all provinces.

17 117. To date, mutual funds in Canada have
18 been essentially conservative in concept and accordingly
19 their shares are appropriate instruments for a broad
20 range of investors. It is logically to be expected
21 however that in the future mutual funds of a more
22 specialized and speculative nature will be formed and
23 indeed such funds could well serve a useful purpose.
24 The investor who is in a position to commit moderate
25 amounts of risk capital in mining or oil enterprises
26 would be provided with the advantages of employing
27 technically qualified specialists at relatively low
28 cost per investor in the investment of the money.

29 118. Initially, mutual funds in Canada were
30 distributed through investment dealers and stock



that in the absence of special regulatory legislation pertaining to investment companies at either or both Federal or provincial levels the various provincial Securities Commissions may be faced with some difficulties in protecting the investing public.

115. It is beyond the scope of this sub-mission to discuss investment company regulations in detail. It is suggested, however, that the Commission should advise that proper provincial legislation provides adequate safeguards for the protection of shareholders of both open and closed end investment trusts.

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117. To date, mutual funds in Canada have been essentially conservative in concept and accordingly their shares are appropriate instruments for a broad range of investors. It is logically to be expected however that in the future mutual funds of a more specialized and speculative nature will be formed and indeed such funds could well serve a useful purpose. The investor who is in a position to commit moderate amounts of risk capital in mining or oil enterprises would be provided with the advantages of employing technically qualified specialists at relatively low cost per investor in the investment of the money.

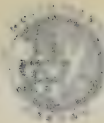
118. Initially, mutual funds in Canada were distributed through investment dealers and stock



brokers who weremembers of the Investment Dealers' Association of Canada and/or Canadian stock exchanges whose salesmen are trained and experienced in the securities business. Today, however, the majority of mutual fund shares are sold by salesmen employed by direct selling organizations.

119. Investor experience in mutual funds has beensatisfactory and there is much public confidence in this form of investment. The attitude has been augmented by Government recognition of mutual fund shares as an acceptable investment for deposit under Registered Retirement Savings Plans of individuals. It is essential that the true concept of the mutual fund be retained in such investment companies if the public is not to be subject to being misled. It may be necessary to introduce legislation at appropriate levels to insure that securities of investment companies were different concepts, regulations and objectives are not offered to the public under the guise of mutual funds.

120. Apprehension has been voiced in regard to the methods employed by some salesmen in marketing of standard dollar "withdrawalplans" as described in paragraphs 71 to 75 inclusive of this submission. The principle involved in these plans is recognized as being a sound and desirable one for those who wish to withdraw some capital gradually, possibly to supplement investment and other revenues. Persons have been persuaded to borrow money from a bank or elsewhere in order to purchase a sufficient number of mutual fund



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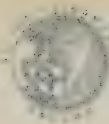
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1 shares to start the plan. As will be appreciated, should
2 the market decline, such a practice could result in a
3 serious loss of capital and financial embarrassment.
4 There are other records of persons liquidating life
5 insurance policies for a similar purpose.

6 121. Some of the literature on "withdrawal
7 plans" base their arguments entirely on past
8 performance. It should be obligatory to state clearly
9 that past performance is not necessarily a guide for
10 the future and that such plans which pay out more than
11 the income earned give a return on capital to the
12 extent that the pay out exceeds net income. It should
13 also be stated most distinctly in the sales literature
14 that plans which guarantee monthly payments pay out so
15 much from income and so much from capital.

16 122. It is appreciated that legislation
17 cannot be substituted satisfactorily for education
18 and experience coupled with voluntary influence in
19 the direction of conduct. Accordingly, the announcement
20 of the formation of a Canadian Association of Investment
21 Companies would seem to be a most constructive
22 development. While it is still in the formative stage,
23 it must be said that an organization of a nature
24 similar to the National Association of Investment
25 Companies in the United States may be expected to make
26 valuable contributions in the maintenance of high
27 standards in the investment company industry as well
28 as assisting both its members in the more technical
29 aspects of the business and the Security Commissions
30 of the various provinces in the introduction and



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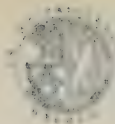
1 administration of legislation pertaining to investment
2 companies.

3 RECOMMENDATION

4 It is recommended to the Commission that
5 consideration be given to the following suggestion:

6 123. That the Commission satisfy itself
7 that there is sufficient protection under existing
8 security acts for the adequate safeguard of share-
9 holders of both open and closed end investment trusts,
10 and if not to make recommendations for any additional
11 regulatory legislation it may deem advisable.

12
13
14 MATERIAL DELETED
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CONFIDENTIAL

Administrative Information

CONFIDENTIAL

RECOMMENDATION

It is recommended to the Commission that consideration be given to the following suggestion: 123. That the Commission satisfy itself that there is sufficient protection under existing security acts for the adequate safeguard of shareholders of both open and closed end investment trusts, and if not to make recommendations for any additional regulatory legislation it may deem advisable.

ADMINISTRATIVE DELETED

MUTUAL FUNDS OPERATING IN CANADA

1. Canadian Incorporations investing essentially in Canada and owned primarily in Canada.

A. BALANCED FUNDS

Investments distributed in varying proportions in common and preferred stocks and corporate and government bonds.

<u>Name</u>	1960 Net <u>Asset Value (z)</u>	Management <u>Fee (y)</u>
	- millions -	
Associate Investors Limited	\$ 0.7	3/10 of 1%Q
Canadian Investment Fund	127.5	1/12 of 1%Q
Champion Mutual Fund of Canada	0.9	1/24 of 1%M
Commonwealth International Corporation	44.5	1/24 of 1%M
Corporate Investors	9.7	1/8 of 1%Q
Federated Growth Fund Ltd.	0.2	1/8 of 1%Q
Fonds Collectif "A" "B" "C"	3.2	N.R.
Investors Mutual of Canada	201.0	1/8 of 1%Q
North American Fund of Canada	6.9	1/8 of 1%Q
Radisson Fund	0.6	1/2 of 1%A
Savings and Investment Corp.		
Mutual Fund of Canada	4.6	1/8 of 1%Q
Timed Investment Fund	<u>1.8</u>	1/8 of 1%Q

B. COMMON STOCK FUNDS

Investments concentrated common stocks (85% or more) nearly all of which are of Canadian corporations.

<u>Name</u>	1960 Net <u>Asset Value (z)</u>	Management <u>Fee (y)</u>
	- millions -	
All-Canadian Compound Fund (x)		1/8 of 1%Q
All-Canadian Dividend Fund	\$ 21.4	1/8 of 1%Q
Dominion Compound Fund	-	3/4 of 1%A
Dominion Dividend Fund	-	3/4 of 1%A
Grouped Income Shares Limited	8.4	1/8 of 1%Q
Investors Growth Fund of Canada Ltd.	46.5	1/8 of 1%Q
Mutual Accumulating Fund	26.0	4/10 of 1%A
Mutual Income Fund (xx)	-	4/10 of 1%A
United Accumulative Fund Ltd.	<u>4.5</u>	1/24 of 1%M
	106.8	

(x) These are recent incorporations.

(xx) Invests only in the shares of Mutual Accumulating Fund.

(y) Expressed as a percentage of net asset value at market.

(z) At market.

Canadian corporations investing essentially in Canada and owned primarily in Canada.

Investments in common and preferred stocks and corporate and government bonds.

Name	Asset Value(z)	1960 Net	Management Fee (%)
	- millions -		
Timed Investment Fund	1.8	4.6	1/3 of 1960
Mutual Fund of Canada			1/8 of 1960
Living and Investment Corp.			1/2 of 1960
Robinson Fund	0.6	6.9	1/8 of 1960
North American Fund of Canada			1/8 of 1960
Investors Mutual of Canada	201.0		1/8 of 1960
Fonds Collective "A" "B" "C"	3.2		1/8 of 1960
Federated Growth Fund Ltd.	0.2		1/8 of 1960
Corporate Investors	9.7		1/8 of 1960
Commonwealth International Corporation	44.5		1/8 of 1960
Chapman Mutual Fund of Canada	0.9		1/8 of 1960
Canadian Investment Fund	127.5		1/12 of 1960
Associate Investors Limited	\$ 0.7		3/10 of 1960

B. COMMON STOCK FUNDS

Investments concentrated common stocks (55%) or more) nearly all of which are of Canadian corporations.

Name	Asset Value(z)	1960 Net	Management Fee (%)
	- millions -		
United Accumulative Fund Ltd.	4.5		1/24 of 1960
Mutual Income Fund (xii)	-		4/10 of 1960
Mutual Accumulating Fund	26.0		4/10 of 1960
Investment Company Fund of Canada Ltd.	46.5		4/10 of 1960
Investment Company Ltd.	11.4		4/10 of 1960
Scotiabank Mutual Fund	-		1/4 of 1960
Dominion Compound Fund	-		3/4 of 1960
All-Canadian Dividend Fund	21.4		1/8 of 1960
All-Canadian Compound Fund (x)			1/8 of 1960

These are recent incorporations. Invests only in the shares of Mutual Accumulating Fund. Expressed as a percentage of net asset value at market.

C. SPECIALTY FUNDS

Mutual Funds that either specialize in certain classes of Canadian securities or whose objectives or features differ from those of the average balanced mutual fund.

<u>Name</u>	<u>1960 Net Asset Value (z)</u> - millions -	<u>Management Fee (y)</u>
Commonwealth International Leverage Fund Ltd.	\$ 4.8	1/2 of 1%A
(fund is permitted to borrow money)		
First Oil and Gas Fund Ltd.	5.3	1/8 of 1%Q
(invests in Canadian petroleum and related industries)		
Growth Oil and Gas	0.2	-
(invests in Canadian oil and gas industry)		
Mutual Bond Fund	1.6	1/10 of 1%Q
Supervised Executive Fund Ltd. (1955)	-	-
1956 Supervised Executive Fund Ltd.	-	-
1957 Supervised Executive Fund Ltd.	-	-
1958 Executive Fund of Canada Ltd.	-	-
	\$11.9	

The 1955, 1956 & 1957 Funds invest only in shares of 1958 Executive Fund which in turn purchases the shares of Supervised Income, Supervised Growth and Supervised American Fund. Investments of 1958 Executive Fund at the end of 1960 were \$813,061.

(z) At market.

(y) Expressed as a percentage of net asset value at market.

2. Mutual Funds incorporated in Canada and investing principally in Canadian stocks but whose shares are distributed largely outside of Canada and held chiefly by European investors.

<u>Name</u>	<u>1960 Net Asset Value (z)</u> - millions -	<u>Management Fee (y)</u>
Beaubran Corporation (French, Swiss and Belgian investors)	\$ 13.9	-
Cana Fund Company Limited (Swiss, Belgian and Dutch investors)	20.1	1%A
Dominion Investments Ltd.	9.0	-
	43.0	

3. Canadian Incorporated Non-Resident Owned Mutual Funds registered under the United States Investment Company Act of 1940. These funds pay no dividends and reinvest all income.

<u>Name</u>	<u>1960 Net Asset Value (z)</u> - millions -	<u>Management Fee (y)</u>
Axe-Templeton Growth Fund of Canada Ltd.	\$ 5.4	1/8 of 1%Q
Canada General Fund Ltd.	71.1	3/32 of 1%Q
Canadian International Growth Fund Ltd.	11.1	3/32 of 1%Q

Classes of Canadian securities or whose objectives or features

EXHIBIT "A"
Page 3

<u>Name</u>	1960 Net	Management
	<u>Asset Value (z)</u>	<u>Fee (y)</u>
	- millions -	
Investors Group Canadian Fund Ltd.	\$119.9	1/8 of 1%Q
Keystone Fund of Canada Ltd.	15.3	3/4 of 1%A
Loomis-Sayles Fund of Canada Ltd.	16.5	5/8 of 1%A
New York Capital Fund, Ltd.	28.7	1/8 of 1%Q
Scudder Fund of Canada, Ltd.	49.9	5/32 of 1%Q
U.B.S. Fund of Canada Ltd.	3.5	5/32 of 1%Q
United Funds Canada Ltd.	15.9	1/2 of 1%A
	\$337.3	

4. Canadian incorporated Mutual Funds held by Canadian investors with investments being made in the United States and Europe.

<u>Name</u>	1960 Net	Management
	<u>Asset Value (z)</u>	<u>Fee (y)</u>
	- millions -	
American Growth Fund Limited	\$ 12.4	1/2 of 1%A
Canadian Growth Fund (x)	-	3/16 of 1%Q
European Growth Fund Limited (x)	-	3/16 of 1%Q
Supervised American Fund	0.2	1/360 of 1%D
	\$12.6	

(x) These are recent incorporations.

(y) Expressed as a percentage of net asset value at market.

(z) At market.

SUMMARY

	<u>Number</u>	1960 Net
		<u>Asset Value</u> <u>(At Market)</u> - millions -
1. Canadian Owned Funds		
A. Balanced	12	\$ 401.6
B. Common Stock Funds	7	106.8
C. Specialty	5	11.9
		\$ 520.3
2. Canadian incorporated - foreign owned funds	3	43.0
3. Canadian NRO Funds registered in U.S.A.	10	337.3
		\$ 900.6
4. Canadian owned Funds for foreign investment	4	\$ 12.6

1980 Net
Asset Value (v)

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Investment
Canadian owned funds for foreign

2.55. 2



EXHIBIT "B"

INCOME TAX ACT

R.S.C. 1952 c. 148 with amendments
Sections 69 and 70

INVESTMENT COMPANIES

69. (1) The tax payable under this part by a corporation for a taxation year when it was an investment company is an amount equal to 18 per cent of its taxable income for the year.

(2) In this Act, "investment company" means a corporation that, in respect of the taxation year in respect of which the expression is being applied, complied with the following conditions:

(a) at least 80 per cent of its property was, throughout the year, shares, bonds, marketable securities or cash.

(b) not less than 95 per cent of its income for the year was derived from investments mentioned in paragraph (a)

*(ba) not less than 85 per cent of its gross revenue for the year was from sources in Canada.

**(bb) not more than 25 per cent of its gross revenue for the year was from interest.

(c) At no time in the year did more than 10 per cent of its property consist of shares, bonds or securities of any one corporation or debtor other than Her Majesty in right of Canada or of



EXHIBIT "B"

INCOME TAX ACT
R.S.C. 1952 c. 148 with amendments
Sections 89 and 90

INVESTMENT COMPANY

89. (1) The tax payable under this part by a corporation for a taxation year when it was an investment company is an amount equal to 18 per cent of its taxable income for the year.

(2) In this Act, "investment company" means a corporation that, in respect of the taxation year in respect of which the expression is being applied,

applies with the following conditions:

(a) at least 80 per cent of its property was, throughout the year, shares, bonds, marketable securities or cash.

(b) not less than 95 per cent of its income for the year was derived from investments mentioned in paragraph (a)

*(ba) not less than 85 per cent of its gross revenue for the year was from sources in Canada.

** (bb) not more than 25 per cent of its gross revenue for the year was from

(c) At no time in the year did more than 10 per cent of its property consist of shares, bonds or securities of any one corporation or debtor other than Her Majesty in right of Canada or of



1 a province or a Canadian municipality.

2 (d) at no time in the year was the
3 number of shareholders of the
4 corporation less than 50, none of
5 whom at any time in the year held
6 more than 25 per cent of the shares of
7 the capital stock of the corporation,
8 and

9 (e) an amount not less than 85 per
10 cent of its taxable income plus exempt
11 income for the year (other than
12 dividends or interests received in
13 the form of shares, bonds or other
14 securities that have not been sold
15 before the end of the taxation year)
16 minus

17 i. 21 per cent of its taxable income
18 for the year and

19 ii. taxes paid in the year to other
20 governments, was distributed to
21 the shareholders before the end
22 of the year.

23 (f) Repealed. 1955, c. 54, s.14(3).

24 (g) Repealed. 1957, c. 29, s.15.

25 * NOTE: Applicable to taxation years commencing in
26 1961 and subsequent taxation years, except that:

27 (a) in the case of a corporation less
28 than 85 per cent but not less than 75
29 per cent of the gross revenue of which
30 for its taxation year commencing in 1960



a province or a Canadian municipality.

(d) at no time in the year was the

number of shareholders of the

corporation less than 50, none of

whom at any time in the year held

more than 25 per cent of the shares of

the capital stock of the corporation,

and

(e) an amount not less than 25 per

cent of its taxable income plus exempt

income for the year (other than

dividends or interests received in

the form of shares, bonds or other

securities that have not been sold

before the end of the taxation year)

minus

1. 21 per cent of its taxable income

for the year and

ii. taxes paid in the year to other

governments, was distributed to

the shareholders before the end

of the year.

(1) Repealed. 1955, c. 54, s. 14(3).

(2) Repealed. 1957, c. 29, s. 15.

* NOTE: Applicable to taxation years commencing in

1961 and subsequent taxation years, except that:

(a) in the case of a corporation less

than 25 per cent but not less than 15

per cent of the gross revenue of which

for its taxation year commencing in 1960



1 was from sources in Canada, the
2 expression "85 per cent" in paragraph
3 (ba) of subsection (2) of section 69
4 as enacted by section 7 of chapter 17
5 of the Statutes of 1960 - 61 shall, in
6 its application to the taxation years
7 of the corporation commencing in 1961
8 and 1962 be read as "75 per cent".
9 (b) in the case of a corporation less
10 than 75 per cent of the gross revenue
11 of which for its taxation year commencing
12 in 1960 was from sources in Canada, the
13 expression "85 per cent" in paragraph
14 (ba) of subsection (2) of section 69
15 an enacted by section 7 of chapter 17
16 of the Statutes of 1960 -- 61 shall,
17 in its application to the taxation year
18 of the corporation commencing in 1961
19 be read as "60 per cent" and in its
20 application to the taxation year of the
21 corporation commencing in 1962, be read
22 as "75 per cent":
23 (c) in the case of a corporation more
24 than 25 per cent but not more than 30
25 per cent of the gross revenue of which
26 for its taxation year commencing in
27 1960 was from interest, the expression
28 "25 per cent" in paragraph (bb) of
29 subsection (2) of section 69 as enacted
30 by section 7 of chapter 17 of the Statutes



by section 7 of chapter 17 of the Statutes
subsection (2) of section 69 as enacted
"25 per cent" in paragraph (bb) of
1960 was from interest, the expression
for its taxation year commencing in
per cent of the gross revenue of which
than 25 per cent but not more than 30
(c) in the case of a corporation more
as "75 per cent":
corporation commencing in 1962, be read
application to the taxation year of the
be read as "60 per cent" and in its
of the corporation commencing in 1961
in its application to the taxation year
of the Statutes of 1960 -- 61 shall,
an enacted by section 7 of chapter 17
(ba) of subsection (2) of section 69
expression "65 per cent" in paragraph
in 1960 was from sources in Canada, the
of which for its taxation year commencing
than 75 per cent of the gross revenue
(b) in the case of a corporation less
and 1962 be read as "75 per cent".
of the corporation commencing in 1961
its application to the taxation year
of the Statutes of 1960 - 61 shall, in
as enacted by section 7 of chapter 17
(ba) of subsection (2) of section 69
expression "85 per cent" in paragraph
was from sources in Canada, the



1 of 1960-61 shall, in its application
2 to the taxation years of the corporation
3 commencing in 1961 and 1962, be read
4 as "30 per cent"; and
5 (d) in the case of a corporation more
6 than 30 per cent of the gross revenue
7 of which for its taxation year commencing
8 1960 was from interest, the expression
9 "25 per cent" in paragraph (bb) of
10 subsection (2) of section 69 as enacted
11 by section 7 of chapter 17 of the
12 Statutes of 1960 -- 61 shall, in its
13 application to the taxation year of
14 the corporation commencing in 1961,
15 be read as "40 per cent" and in its
16 application to the taxation year of
17 the corporation commencing in 1962,
18 be read as "30 per cent". (1960-61,
19 c. 17.s.7 (2).)
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NON-RESIDENT-OWNED INVESTMENT CORPORATION

70. (1) In computing the taxable income of

a non-resident-owned investment corporation for a taxation year, notwithstanding Division 5, no deduction may be made from its income for the year except

(a) dividends and interest received in the year from other non-resident-owned investment corporation, and

(b) taxes paid to the Government of a country other than Canada in respect of any part of the income of the corporation for the year derived from

interest-bearing

and in computing its income no deduction shall be made in respect of interest on its bonds, debentures, securities or other indebtedness and no deduction shall be made under paragraph (b) of subsection (1) of section 11 or subsection (2) of section 11.

(2) The tax payable under this Part by a corporation for a taxation year when it was a non-resident-owned investment corporation is an amount equal to 15 per cent of its taxable income for the year.

(3) No deduction from the tax payable under this Part by a non-resident-owned investment corporation may be made under Section 40 or in respect of tax paid to the government of a country other than Canada.

(4) In this Act, a "non-resident-owned investment corporation" means a corporation incorporated in Canada that during the whole of the taxation year in respect of which the expression is being applied



1 complied with the following conditions:

2 (a) at least 95 per cent of the aggregate
3 value of its issued shares and all of
4 its bonds, debentures and other funded
5 indebtedness were

6 i. beneficially owned by non-
7 resident persons,

8 ii. owned by trustees for the
9 benefit of non-resident persons
10 or their unborn issue, or
11 iii. owned by a corporation, whether
12 incorporated in Canada or elsewhere,
13 at least 95 per cent of the

14 aggregate value of the issued
15 shares of which and all of the
16 bonds, debentures and other
17 funded indebtedness of which
18 where beneficially owned by non-
19 resident persons or owned by
20 trustees for the benefit of non-
21 resident persons or their unborn
22 issue or by several such
23 corporations;

24 (b) its income was derived from

25 i. ownership of or trading or
26 dealing in bonds, shares,
27 debentures, mortgages, hypothecs,
28 bills, notes or any interest
29 therein,
30



complied with the following conditions:

(a) at least 95 per cent of the aggregate

value of its issued shares and all of

its bonds, debentures and other funded

indebtedness were

i. beneficially owned by non-

resident persons,

ii. owned by trustees for the

benefit of non-resident persons

or their unborn issue, or

iii. owned by a corporation, whether

incorporated in Canada or elsewhere,

at least 95 per cent of the

aggregate value of the issued

shares of which and all of the

bonds, debentures and other

funded indebtedness of which

were beneficially owned by non-

resident persons or owned by

trustees for the benefit of non-

resident persons or their unborn

issue or by several such

corporations;

(b) its income was derived from

i. ownership of or trading on

dealing in bonds, shares,

insurance, and other securities;

ii. bills, notes or any interest



11. lending money with or

without security.

iii. rents, hire of chattels,

charterparty fees or

remunerations, annuities,

royalties, interest or

dividends, or

iv. estates or trusts;

(ba) not more than 10 per cent of its gross revenue was derived from rents, hire of chattels, charterparty fees or charterparty remunerations.

(c) its principal business was not

i. the making of loans, or

ii. trading or dealing in mortgages,

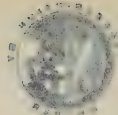
hypothecs, bills, notes or

other similar property or any

interest therein;

(d) it has, not later than 90 days after the commencement of the taxation year, elected in prescribed manner to be taxed under this section; and

(e) it has not, before the taxation year, revoked in a prescribed manner the elections so made by it. 1948, c.52, s.63; 1949 (2nd Sess.), c.25, s.32; 1952, c.29, s.20.



11. lending money with or
without security.
111. rents, hire of chattels,
charterparty fees or
remunerations, annuities,
royalties, interest or
dividends, or
iv. estates or trusts;
(b) not more than 10 per cent of its gross
revenue was derived from rents, hire of
chattels, charterparty fees or charterparty
remunerations.
(c) its principal business was not
1. the making of loans, or
11. trading or dealing in mortgages,
hypothecs, bills, notes or
other similar property or any
interest therein;
(d) it has, not later than 90 days after the
commencement of the taxation year, elected
in prescribed manner to be taxed under this
section; and
(e) it has not, before the taxation year,
revoked in a prescribed manner the elections
so made by it. 1948, c. 52, s. 63; 1949
(Tax Consol.) s. 65; 1952, c. 49, s. 70.

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- 50 -

EXHIBIT " "
PAGE: 1

AN ANALYSIS OF THE FIRST FIFTEEN COMMON STOCKS HAVING
BOTH A BID AND ASKED PRICE IN THE MONTREAL STOCK EXCHANGE
OFFICIAL DAILY NEWS AS OF THE CLOSE OF BUSINESS SHOWING
THE DIFFERENCE BETWEEN THE TOTAL COST OF SHARES PURCHASED
AT THE ASKED PRICES, AND THE PROCEEDS WHEN THEY ARE SOLD AT THE BID PRICES

	Asked Price Per Sh.	Comm- ission	Shares Bought	Total Cost	Bid Price Per Sh.	Comm- ission	Net Proceeds
<u>As at May 31, 1960</u>							
Alcan	\$41-1/4	\$0.40	240.0	\$10,000	\$40-3/4	\$0.40	\$ 9,684
Alcan Atl. Sugar	10-1/4	0.25	952.3	10,000	9-3/4	0.20	9,094
Alcan Surpass Shoe	19	0.30	518.1	10,000	18	0.30	9,170
Alcan Steel	35	0.35	282.8	10,000	34-3/4	0.35	9,728
Alcanium Ltd.	32-3/8	0.35	305.5	10,000	32-1/8	0.35	9,707
Alcan Corp.	30-1/8	0.35	328.1	10,000	30	0.35	9,728
Alcan Corp.	25	0.35	394.4	10,000	24-1/2	0.30	9,544
Alcan Steels	22	0.30	448.4	10,000	20-1/8	0.30	9,058
Alcan of Montreal	51	0.40	194.5	10,000	50-1/2	0.40	9,744
Alcan of Nova Scotia	62-3/4	0.45	158.2	10,000	62-1/4	0.45	9,777
Alcan.Cdn.Nationale	51	0.40	194.5	10,000	50-1/2	0.40	9,744
Alcan. Provinciale	35	0.35	282.8	10,000	33-3/4	0.35	9,446
Alcanhurst P.& P."A"	44	0.40	225.2	10,000	43-1/4	0.40	9,650
Alcanhurst P.& P."B"	33	0.35	299.8	10,000	32	0.35	9,489
Alcan Telephone	45	0.40	220.2	10,000	44-3/4	0.40	9,766

\$150,000\$143,330SUMMARY

15 Common Stocks

Total Cost	\$150,000
Net Proceeds	143,330
"Spread"	<u>\$ 6,670</u>
Percentage "Spread"	<u>4.45%</u>

As at April 29, 1960

Alcan	\$38-1/4	\$0.35	259.1	\$10,000	\$38	\$0.35	\$ 9,755
Alcan Surpass Shoe	19-1/4	0.30	511.5	10,000	18-5/8	0.30	9,373
Alcan Steel	33-3/4	0.35	293.25	10,000	33	0.35	9,575
Alcanium Ltd.	28-3/4	0.35	343.6	10,000	28-5/8	0.35	9,715
Alcan Corp.	32	0.35	309.1	10,000	28-1/8	0.35	8,585
Alcan Corp.	26	0.35	379.5	10,000	24-1/2	0.30	9,184
Alcan Steels	23-1/2	0.30	420.1	10,000	23	0.30	9,536
Alcan of Montreal	49-3/4	0.40	199.4	10,000	49-1/4	0.40	9,741
Alcan of Nova Scotia	60	0.45	165.4	10,000	59-3/4	0.40	9,816
Alcan.Cdn.Nationale	50-1/2	0.40	196.4	10,000	49-1/2	0.40	9,643
Alcan. Provinciale	36	0.35	275.1	10,000	35	0.35	9,532
Alcanhurst P.& P."A"	45	0.40	220.2	10,000	44	0.40	9,601
Alcanhurst P.& P."B"	32-1/2	0.35	304.4	10,000	31	0.35	9,330
Alcan Telephone	44-5/8	0.40	222.0	10,000	44-1/2	0.40	9,790
Alcan Paper	8	0.20	1,219.5	10,000	7-1/2	0.20	8,902

\$150,000\$142,079SUMMARY

15 Common Stocks

Total Cost	\$150,000
Net Proceeds	142,079
"Spread"	<u>\$ 7,921</u>
Percentage "Spread"	<u>5.28%</u>

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\$150,000
Total Cost
\$150,000
Spread

As of April 29, 1960

Percentage "Spreads" 1970-1971

AN ANALYSIS OF THE FIRST FIFTEEN COMMON STOCKS HAVING
BOTH A BID AND ASKED PRICE IN THE MONTREAL STOCK EXCHANGE
OFFICIAL DAILY NEWS AS OF THE CLOSE OF BUSINESS SHOWING
THE DIFFERENCE BETWEEN THE TOTAL COST OF SHARES PURCHASED
AT THE ASKED PRICES, AND THE PROCEEDS WHEN THEY ARE SOLD AT THE BID PRICES

	Asked Price Per Sh.	Comm- ission	Shares Bought	Total Cost	Bid Price Per Sh.	Comm- ission	Net Proceeds
As at June 21, 1957							
New Surpass Shoe	\$ 8	\$0.20	1,234.5	\$10,000	\$ 7-3/4	\$0.20	\$ 9,320
Aluminum Ltd.	44-1/2	0.40	222.7	10,000	44-1/4	0.40	9,765
Imperial Corp.	17	0.30	578.0	10,000	16-1/2	0.30	9,364
Bestos Corp.	31-1/2	0.35	313.9	10,000	31	0.35	9,621
Las Steels	25-3/4	0.35	383.1	10,000	25	0.35	9,712
Bank of Montreal	47-3/8	0.40	209.3	10,000	47	0.40	9,753
Bell Telephone	40-7/8	0.40	242.2	10,000	40-3/4	0.40	9,773
Canadian Traction	9-3/4	0.20	1,005.0	10,000	9-1/2	0.20	9,347
A. Oil	53-1/4	0.40	186.3	10,000	52-1/4	0.40	9,660
E. Power	51-1/2	0.40	192.6	10,000	51	0.40	9,746
E. Telephone	44	0.40	225.2	10,000	43-1/2	0.40	9,706
Stuck Mills "A"	7	0.15	1,398.6	10,000	6-1/2	0.15	8,881
Stuck Mills "B"	2-3/4	0.06	3,558.7	10,000	2	0.06	6,904
Building Products	35	0.35	282.8	10,000	33	0.35	9,233
Colo Gold Dredging	4.00	0.10	2,439.0	10,000	3.75	0.08	8,951

\$150,000\$139,736

SUMMARY

15 Common Stocks

Total Cost \$150,000
 Net Proceeds 139,736
 "Spread" \$ 10,264
 Percentage "Spread" 6.84%

As at November 2, 1956

Atlatl	\$34-5/8	\$0.35	285.9	\$10,000	\$34-1/2	\$0.35	\$ 9,763
Atlatl Atl. Sugar	8-5/8	0.20	1,133.2	10,000	8-1/2	0.20	9,406
Atlatl Steel	111	0.60	89.6	10,000	110	0.60	9,802
Aluminum Ltd.	121	0.60	82.25	10,000	119-3/4	0.60	9,800
Imperial Corp.	18-1/2	0.30	531.9	10,000	17-3/4	0.30	9,282
Bestos Corp.	37	0.35	267.75	10,000	35-1/2	0.35	9,411
Las Steels	29-1/2	0.35	335.1	10,000	29-1/4	0.35	9,684
Bank of Montreal	50	0.40	198.5	10,000	49-1/2	0.40	9,746
Bank of Nova Scotia	55-1/2	0.40	178.9	10,000	55	0.40	9,768
Bank of Canada	40-1/2	0.40	244.5	10,000	40	0.40	9,682
Bell Telephone	45-7/8	0.40	216.1	10,000	45-5/8	0.40	9,773
Canadian Traction	7-1/2	0.20	1,298.7	10,000	7-3/8	0.15	9,383
A. Bank Note	35	0.35	282.9	10,000	30	0.35	8,388
A. Oil Co.	46	0.40	215.6	10,000	45-3/4	0.40	9,777
C. Forest Prod.	13-1/4	0.25	740.75	10,000	13	0.25	9,445

\$150,000\$143,112

SUMMARY

15 Common Stocks

Total Cost \$150,000
 Net Proceeds 143,112
 "Spread" \$ 6,888
 Percentage "Spread" 4.59%

ALL THE STOCKS LISTED IN THE MONTREAL STOCK EXCHANGE
 BOTH A BID AND ASKED PRICE IN THE MONTREAL STOCK EXCHANGE
 OFFICIAL DAILY NEWS AS OF THE CLOSE OF BUSINESS SHOWING
 THE BID AND ASKED PRICES, AND THE PROCEEDS WHEN THEY ARE SOLD AT THE BID PRICES

Per Sh.	Session	Boards	Cost	Per Sh.	Session	Boards
As at June 21, 1927						
\$ 8	\$0.20	1,234.2	\$10,000	\$ 7-3/4	\$0.20	\$ 9,320
17	0.30	278.0	10,000	16-1/2	0.70	9,304
31-1/2	0.35	313.0	10,000	31	0.35	9,621
25-3/4	0.35	283.1	10,000	25	0.35	9,712
47-3/8	0.40	200.3	10,000	47	0.40	9,722
40-7/8	0.40	242.3	10,000	40-3/4	0.40	9,723
9-3/4	0.20	1,002.0	10,000	9-1/2	0.20	9,347
23-1/4	0.40	180.3	10,000	23-1/4	0.40	9,680
21-1/2	0.40	125.6	10,000	21	0.40	9,740
44	0.40	252.3	10,000	43-1/2	0.40	9,706
7	0.15	1,308.6	10,000	6-1/2	0.15	9,881
2-3/4	0.00	3,288.7	10,000	2	0.00	9,694
25	0.35	382.8	10,000	23	0.35	9,725
4.00	0.10	2,423.0	10,000	3.75	0.08	9,121
\$120,000						

12 Common Stocks

Total Cost \$120,000
 Net Proceeds \$120,735

As at November 2, 1926

\$24-5/8	\$0.35	282.0	\$10,000	\$24-1/2	\$0.35	\$ 9,767
8-5/8	0.20	1,133.3	10,000	8-1/2	0.20	9,406
111	0.60	83.6	10,000	110	0.60	9,405
121	0.60	83.25	10,000	110-3/4	0.60	9,407
37	0.35	267.75	10,000	35-1/2	0.35	9,711
29-1/2	0.35	323.1	10,000	29-1/4	0.35	9,443
25-1/2	0.40	174.0	10,000	25	0.40	9,726
46	0.35	282.9	10,000	45-3/4	0.35	9,727
46	0.40	212.6	10,000	45-3/4	0.40	9,727

12 Common Stocks

Total Cost \$120,000
 Net Proceeds \$120,715

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STATISTICAL SUMMARY OF OPEN-END
UNITED STATES
INVESTMENT COMPANIES (MUTUAL FUNDS)

<u>Year</u>	<u>No. of Companies Reporting</u>	<u>Total (1) Net Assets (\$000)</u>	<u>Share- holder (1) Accts. In Force</u>	<u>Sold</u>	<u>Shares Redeemed (\$000)</u>	<u>% Red. to Sales</u>
1940	68	447,959	295,056	N. A.	N. A.	-
1941	68	401,611	293,251	53,312	45,024	84.4
1942	68	468,580	312,609	73,140	25,440	34.8
1943	68	653,653	341,435	116,062	51,221	44.1
1944	68	882,191	421,675	169,228	70,815	41.8
1945	73	1,284,185	497,875	292,359	109,978	37.6
1946	74	1,311,108	580,221	370,353	143,612	38.8
1947	80	1,409,165	672,543	266,924	88,732	33.2
1948	87	1,505,762	722,118	273,787	127,171	46.4
1949	91	1,973,547	842,198	385,526	107,587	27.9
1950	98	2,530,563	938,651	518,811	280,728	54.1
1951	103	3,129,629	1,110,432	674,610	321,550	47.7
1952	110	3,931,407	1,359,000	782,902	196,022	25.0
1953	110	4,146,061	1,537,250	672,005	238,778	35.5
1954	115	6,109,390	1,703,846	862,817	399,702	46.3
1955	125	7,837,524	2,085,325	1,207,458	442,550	36.6
1956	135	9,046,431	2,580,049	1,346,738	432,750	32.1
1957	143	8,714,143	3,110,392	1,390,557	405,716	29.2
1958	151	13,242,388	3,630,096	1,619,768	511,263	31.6
1959	155	15,817,962	4,276,077	2,279,982	785,627	34.4
1960	161	17,025,684	4,897,600	2,097,246	841,815	40.1

(1) At year end.

Source Material: National Association of Investment Companies.

STATISTICAL SUMMARY OF OPEN-END
UNITED STATES
INVESTMENT COMPANIES (MUTUAL FUNDS)

Year	No. of Companies Reporting	Assets (\$'000)	Total (1) Net Assets	Share- holder (1) In Force	Shares (\$'000)	% of Assets
1949	91	1,973,347	842,198	382,526	107,587	27.9
1948	87	1,502,782	722,118	273,787	124,171	46.4
1947	80	1,409,182	672,243	266,924	88,732	33.2
1946	74	1,311,109	580,221	270,323	143,612	38.8
1945	73	1,284,182	497,872	232,329	102,978	37.6
1944	68	882,191	421,672	169,228	70,812	41.8
1943	66	623,623	341,432	116,062	51,221	44.1
1942	68	468,280	212,609	73,140	22,440	34.9
1941	68	401,611	293,221	53,312	42,024	84.4
1940	68	447,929	292,026			
1939	161	17,022,684	4,897,600	2,027,246	841,812	40.1
1938	152	12,817,962	4,276,077	2,279,982	782,622	34.4
1937	143	8,714,143	3,110,392	1,290,227	402,716	30.2
1936	121	9,240,472	2,460,000	1,146,000	412,746	12.1
1935	122	7,837,224	2,082,322	1,207,428	442,220	36.6
1934	112	6,109,390	1,703,846	862,817	399,702	46.3
1933	110	4,146,061	1,237,220	672,002	238,778	35.2
1932	110	3,931,407	1,229,000	782,902	196,022	25.0
1931	103	3,129,629	1,110,432	674,610	321,220	47.7
1930	98	2,230,263	938,621	518,811	280,728	54.1

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EIGHT LARGEST U.S. DOMESTIC OPEN-END FUNDS

	*	Net Assets at Market					Shares Outstanding (x)						
		1960	1959	1958	1957	1956	1955	1960	1959	1958	1957	1956	1955
		-	-	-	-	-	-	-	-	-	-	-	-
		-	-	-	-	millions	-	-	-	-	millions	-	-
1. Affiliated Fund	1934	586	575	478	346	358	336	82.9	76.1	68.8	63.1	60.1	55.6
2. Fundamental Investors	1932	591	599	515	335	372	320	66.2	62.0	56.4	50.1	45.0	40.9
3. Investors Mutual	1940	1,505	1,413	1,217	997	954	847	150.4	138.6	125.3	116.6	104.8	93.2
4. Investors Stock Fund	1945	638	559	380	233	205	133	41.6	33.9	24.9	19.9	15.4	10.9
5. Massachusetts Invest. Trust	1924	1,508	1,558	1,432	976	1,098	957	114.5	111.8	107.3	100.5	94.5	87.3
6. National Securities Series	1940	440	467	388	276	284	249	76.2	70.4	65.4	54.3	41.7	36.4
7. United Funds, Inc.	1940	863	748	559	342	349	273	73.4	62.2	50.5	40.7	33.1	27.3
8. Wellington Fund	1928	1,087	1,017	858	604	579	497	81.0	71.9	61.8	52.3	44.6	37.2
		7,218	6,936	5,827	4,109	4,199	3,612	686.2	626.9	560.4	497.5	439.2	388.8

(x) Adjusted for stock splits.

Date of Incorporation.

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ILLUSTRATION OF WITHDRAWAL PLAN
1950 - 1961
 (discussed in paras. 71-75)

ELEVEN YEAR (PLUS 10 MONTHS) SUMMARY OF \$25,000
INVESTED IN INVESTORS MUTUAL OF CANADA LTD.* ON MARCH 1, 1950
AND MONTHLY REDEMPTIONS OF \$200.00 COMMENCING
ONE YEAR AFTER ORIGINAL INVESTMENT

ALL DIVIDENDS RE-INVESTED

March 1, 1950 - Original Investment	\$25,000.00
(4,672,897 shares @ \$5.35)	
Total Dividends Re-invested (11 years, 10 months)	\$14,306.20
Total Redemptions	
(130 x \$200) (10 years, 10 months)	\$26,000.00
December 31, 1961 - Value of Remaining Shares	
(3,371,649 x \$13.356)	\$45,031.74

* Extract from Company's literature which also carries the following statement:

"WHILE THE FOREGOING FIGURES ARE BASED ON ACTUAL PAST PERFORMANCE THEY CANNOT BE CONSTRUED AS AN INDICATION OR GUARANTEE OF FUTURE PERFORMANCE".

SUMMARY OF ACCOUNT AS AT DECEMBER 31 OF EACH YEAR

March 1, 1950 - Original Investment	\$25,000.00
(4,672,897 shares @ \$5.35)	

<u>Dec. 31,</u>	<u>Number of Shares</u>	<u>Price per Share</u>	<u>Value</u>
1950	4,783.148	5.750	27,503.10
1951	4,679.923	6.490	30,372.70
1952	4,506.600	6.431	28,981.94
1953	4,326.335	6.395	27,666.91
1954	4,159.718	8.379	34,854.28
1955	4,029.292	9.710	39,124.43
1956	3,912.979	10.112	39,568.04
1957	3,798.411	8.950	33,995.78
1958	3,675.277	11.117	40,858.05
1959	3,568.972	11.219	40,040.30
1960	3,463.626	11.368	39,374.50
1961	3,371.649	13.356	45,031.74

STATEMENT OF THE INVESTMENT
1950 - 1951
ASSETS

THIS STATEMENT IS IN ACCORDANCE WITH THE BY-LAWS OF THE INVESTMENT MUTUAL OF CANADA LTD. ON MARCH 1, 1950
 AND MONTHLY REDEMPTIONS OF \$25.00 COMMENCING
 ONE YEAR AFTER ORIGINAL INVESTMENT

ALL DIVIDENDS RE-INVESTED

March 1, 1950 - Original Investment \$25,000.00
 (4,672.897 shares @ \$5.35)
 Total Dividends Re-invested (11 years, 10 months) \$14,306.20
 Total Redemptions (10 x \$25.00) (10 years, 10 months) \$2,500.00
 December 31, 1961 - Value of Remaining Shares \$42,037.74
 (3,371,649 x \$12.35)

* Extract from Company's literature which also carries the following statement:

"WHILE THE FOREGOING FIGURES ARE BASED ON ACTUAL PAST PERFORMANCE THEY CANNOT BE CONSIDERED AS AN INDICATION OR GUARANTEE OF FUTURE PERFORMANCE."

SUMMARY OF ACCOUNT AS AT DECEMBER 31 OF EACH YEAR

March 1, 1950 - Original Investment \$25,000.00
 (4,672.897 shares @ \$5.35)

<u>Dec. 31,</u>	<u>Number of shares</u>	<u>Price per share</u>	<u>Value</u>
1950	4,672.897	\$5.35	\$25,000.00
1951	4,672.897	\$5.35	\$25,000.00
1952	4,608.600	\$5.41	\$25,000.00
1953	4,544.403	\$5.47	\$25,000.00
1954	4,480.206	\$5.53	\$25,000.00
1955	4,416.009	\$5.59	\$25,000.00
1956	4,351.812	\$5.65	\$25,000.00
1957	4,287.615	\$5.71	\$25,000.00
1958	4,223.418	\$5.77	\$25,000.00
1959	4,159.221	\$5.83	\$25,000.00
1960	4,095.024	\$5.89	\$25,000.00
1961	4,030.827	\$5.95	\$25,000.00
1962	3,966.630	\$6.01	\$25,000.00
1963	3,902.433	\$6.07	\$25,000.00
1964	3,838.236	\$6.13	\$25,000.00
1965	3,774.039	\$6.19	\$25,000.00
1966	3,709.842	\$6.25	\$25,000.00
1967	3,645.645	\$6.31	\$25,000.00
1968	3,581.448	\$6.37	\$25,000.00
1969	3,517.251	\$6.43	\$25,000.00
1970	3,453.054	\$6.49	\$25,000.00
1971	3,388.857	\$6.55	\$25,000.00
1972	3,324.660	\$6.61	\$25,000.00
1973	3,260.463	\$6.67	\$25,000.00
1974	3,196.266	\$6.73	\$25,000.00
1975	3,132.069	\$6.79	\$25,000.00
1976	3,067.872	\$6.85	\$25,000.00
1977	3,003.675	\$6.91	\$25,000.00
1978	2,939.478	\$6.97	\$25,000.00
1979	2,875.281	\$7.03	\$25,000.00
1980	2,811.084	\$7.09	\$25,000.00
1981	2,746.887	\$7.15	\$25,000.00
1982	2,682.690	\$7.21	\$25,000.00
1983	2,618.493	\$7.27	\$25,000.00
1984	2,554.296	\$7.33	\$25,000.00
1985	2,490.099	\$7.39	\$25,000.00
1986	2,425.902	\$7.45	\$25,000.00
1987	2,361.705	\$7.51	\$25,000.00
1988	2,297.508	\$7.57	\$25,000.00
1989	2,233.311	\$7.63	\$25,000.00
1990	2,169.114	\$7.69	\$25,000.00
1991	2,104.917	\$7.75	\$25,000.00
1992	2,040.720	\$7.81	\$25,000.00
1993	1,976.523	\$7.87	\$25,000.00
1994	1,912.326	\$7.93	\$25,000.00
1995	1,848.129	\$7.99	\$25,000.00
1996	1,783.932	\$8.05	\$25,000.00
1997	1,719.735	\$8.11	\$25,000.00
1998	1,655.538	\$8.17	\$25,000.00
1999	1,591.341	\$8.23	\$25,000.00
2000	1,527.144	\$8.29	\$25,000.00
2001	1,462.947	\$8.35	\$25,000.00
2002	1,398.750	\$8.41	\$25,000.00
2003	1,334.553	\$8.47	\$25,000.00
2004	1,270.356	\$8.53	\$25,000.00
2005	1,206.159	\$8.59	\$25,000.00
2006	1,141.962	\$8.65	\$25,000.00
2007	1,077.765	\$8.71	\$25,000.00
2008	1,013.568	\$8.77	\$25,000.00
2009	949.371	\$8.83	\$25,000.00
2010	885.174	\$8.89	\$25,000.00
2011	820.977	\$8.95	\$25,000.00
2012	756.780	\$9.01	\$25,000.00
2013	692.583	\$9.07	\$25,000.00
2014	628.386	\$9.13	\$25,000.00
2015	564.189	\$9.19	\$25,000.00
2016	500.000	\$9.25	\$25,000.00

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CANADIAN INVESTMENT FUND, LTD.

<u>Year</u>	<u>No. Shares Issued</u>	<u>No. Shares Redeemed</u>	<u>No. Shares Outstanding</u>	<u>Total Net Assets</u>	<u>No. of Share- holders</u>
1933	242,004	NIL	242,004	733,771	N.A.
1934	503,929	NIL	745,933	2,473,785	N.A.
1935	248,749	86,720	907,962	3,593,667	N.A.
1936	299,170	66,800	1,140,332	5,496,068	N.A.
1937	507,106	NIL	1,647,438	5,819,789	3,205
1938	509,204	1,000	2,155,642	8,990,290	4,351
1939	329,242	95,749	2,389,135	10,002,339	4,772
1940	103,021	217,410	2,274,746	7,829,966	4,784
1941	114,757	97,790	2,291,713	7,164,996	4,815
1942	200,580	18,982	2,473,311	8,255,541	4,952
1943	87,862	27,638	2,533,535	9,370,107	5,061
1944	166,135	24,949	2,674,721	10,993,437	5,216
1945	49,717	167,299	2,557,139	12,982,480	5,126
1946	129,497	166,318	2,520,318	11,862,364	5,141
1947	228,705	25,192	2,723,831	12,554,079	5,781
1948	411,920	32,450	3,013,301	14,452,824	6,325
1949	1,988,451	13,732	5,078,020	25,318,567	10,398
1950	1,672,608	13,533	6,731,095	39,277,667	14,133
1951	296,070	90,754	6,942,411	44,561,661	15,059
1952	295,178	54,269	7,183,320	45,718,056	16,171
1953	496,462	22,821	7,656,961	45,803,482	17,005
1954	817,645	340,036	8,134,570	63,843,602	17,636
1955	704,019	65,106	8,773,483	79,335,996	18,260
1956	902,667	45,592	9,630,558	86,720,977	19,409
1957	1,285,462	110,736	10,805,284	83,821,628	20,706
1958	2,265,651	58,952	13,011,983	120,195,297	23,651
1959	1,191,255	231,696	13,971,542	126,632,665	24,687
1960	754,820	339,441	14,386,921	127,466,674	24,786
1961	554,841	919,500	14,022,262	151,207,107	23,423

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INVESTORS MUTUAL OF CANADA LTD.

<u>Fiscal Year Ended Oct. 31</u>	<u>Shares Issued</u>	<u>Shares Redeemed</u>	<u>Shares Outstanding</u>	<u>Number of Share- holders</u>
1950	465,957.590	602.720	465,354.870	1,801
1951	1,368,639.280	50,579.620	1,783,414.530	6,086
1952	1,399,583.380	108,610.560	3,074,387.350	9,862
1953	1,644,376.210	183,940.280	4,534,823.280	13,358
1954	1,859,376.770	389,232.660	6,004,967.390	16,187
1955	3,149,463.260	373,193.260	8,781,237.390	23,196
1956	3,514,894.800	585,529.436	11,710,402.754	32,585
1957	3,096,183.693	929,231.217	13,877,355.230	40,168
1958	2,361,522.447	1,081,274.226	15,157,603.451	41,768
1959	3,359,443.735	1,192,004.981	17,325,042.205	44,267
1960	2,949,714.776	1,344,969.885	18,929,787.096	45,409
1961	4,059,905.075	1,422,744.234	21,566,947.937	51,700

CANADIAN INCORPORATED N.R.O. MUTUAL FUNDS

PRIMARILY OWNED IN U.S.A.

	Net Value Assets at Market						Total Shares Outstanding					
	1960	1959	1958	1957	1956	1955	1960	1959	1958	1957	1956	1955
*	-	-	-	-	-	-	-	-	-	-	-	-
	-	-	-	\$ millions	-	-	-	-	-	\$ millions	-	-
Axe Templeton Growth	5.4	4.1	3.5	3.0	5.8	-	.62	.58	.55	.61	1.0	(x)
Canada General Fund	71.1	89.1	91.1	73.6	65.6	54.6	5.4	6.4	6.5	6.6	5.6	5.5
Cdn. Int. Growth	11.1	10.2	6.5	4.5	-	-	1.1	1.0	.78	.73	-	-
Investors Group Cdn.	111.9	144.2	167.4	120.3	107.9	51.6	21.1	25.7	29.3	27.9	19.1	10.2
Keystone Fund of Cda.	15.3	16.3	14.6	12.6	8.8	6.4	1.1	1.3	1.2	1.2	.88	.71
N.Y. Capital Fund	28.7	31.1	28.1	23.0	27.8	27.5	2.1	2.4	2.3	2.5	2.6	2.9 (x)
Scudder Fund Canada	49.9	55.4	59.7	45.0	49.7	50.1	4.2	4.7	5.0	4.7	4.8	5.0 (x)
United Funds Canada	15.9	18.5	23.3	19.1	20.7	14.4	.97	1.2	1.5	1.3	1.3	.99
	\$309	\$369	\$394	\$301	\$286	\$205	36.6	43.3	47.1	45.5	35.3	25.3

* Date of incorporation.

(x) Adjusted for stock splits.

Loomis-Say's Fund of Canada Ltd. and U.B.S. Fund of Canada Ltd. have been omitted from the above tabulation because they are recent incorporations and would distort the overall figures.



Nethercut & Young

Toronto, Ontario

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APPENDIX L

FINANCING OF SMALL BUSINESSES

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University of Toronto
Toronto, Ontario

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APPENDIX I

FINANCING OF SMALL BUSINESSES

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FINDINGS OF THE COMMITTEE INVESTIGATING
THE FINANCING OF SMALL BUSINESSES FOR
THE INVESTMENT DEALERS' ASSOCIATION'S
BRIEF TO THE ROYAL COMMISSION

DEFINITION

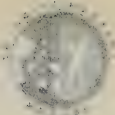
1) The sponsors of a worthwhile project requiring financing of \$500,000 or more can generally make satisfactory arrangements for either a debt or equity issue with an established investment dealer. For the purposes of this study therefore, a small business is defined as one requiring to raise less than \$500,000 regardless of the size of the business itself. Generally speaking a large business will not be looking for less than \$500,000 through other than banking or regular mortgage channels.

WAYS OPEN TO A SMALL BUSINESS IN SECURING FINANCING

Private Placement

2) Friends and relatives of the entrepreneur who may take shares or bonused notes. This is the common approach for the very small enterprise and for the fortunate few having the right contacts. Private placements of both debt and equity can sometimes be arranged through investment dealers who will place the issue with a small group of clients or with one or two institutions selected from among the few willing to participate in financing of this type. Occasionally the members of the dealer firm will themselves participate if the issue particularly appeals to them or if it is a piece of interim financing before the company is ready for public offering.

3) Unfortunately, the record shows that few



FINDINGS OF THE COMMITTEE INVESTIGATING
THE FINANCING OF SMALL BUSINESSES FOR
THE FUTURE
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3) Unfortunately, the record shows that few



1 companies can qualify for this type of financing. In
2 a recent survey made for the purposes of this study,
3 47 of the 103 Investment Dealers' Association members
4 reporting had offered a total of 217 small business
5 issues during the past two years. Of this number
6 only 18 were for private placement.

7 Industrial Development Bank

8 4) This is Canada's best answer to date to the
9 problem under study. At the end of its latest fiscal
10 year the Bank had 1,364 loans outstanding for a total
11 amount of \$71,196,000 indicating an average outstanding
12 balance of \$52,000 per loan. Loans are only granted
13 on the security of fixed assets.

14 5) In connection with the I.D.B. operations
15 the following criticisms were encountered:

16 i. Services too slow

17 ii. Costs, which sometimes include bonus
18 shares, may be too high as evidenced
19 by the fact that reserves of some \$18
20 million have been accumulated by the Bank.

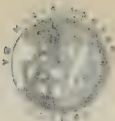
21 iii. The lien on assets is often too tight
22 or too wide to permit secondary financing.

23 iv. The required ratio of equity to the
24 proposed loan may be too high.

25 v. The small business is often obliged
26 to accept fixed obligations when equity
27 capital may have been the proper route.

28 vi. Repayment requirements are often
29 too heavy in the early years.

30 The Committee did not consider it incumbent upon it to



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Industrial Development Bank

1) This is the Bank's first survey to date on the problem under study. At the end of its latest fiscal year the Bank had 1,304 loans outstanding for a total amount of \$1,190,000 indicating an average outstanding balance of \$52,000 per loan. Loans are only granted on the security of fixed assets.

2) In connection with the I.D.B. operations the following criticisms were encountered:

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- ii. Loans, which sometimes require longer shares, may be too high as evidenced by the fact that reserves of some \$18 million have been accumulated by the Bank.
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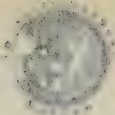


1 investigate these criticisms and in general has felt
2 that the operations of the I.D.B. were satisfactory.

3 Chartered Banks

4 6) This should be the first stop for the
5 business requiring short term loans for such purposes as
6 carrying inventory, accounts receivable, etc. This
7 aspect is outside the scope of this study but it should
8 be noted that inexperienced managements sometimes over-
9 look this source of funds. Of particular importance
10 are the bank loans available under the terms of the Small
11 Business Loans Act. Manufacturing, wholesale trade,
12 retail trade and service businesses grossing less than
13 \$250,000 per year may borrow up to \$25,000 for certain
14 kinds of equipment, fixed assets or improvements to
15 fixed assets. The loan may cover up to 80 per cent of
16 the cost (90 per cent on improvements to premises).
17 The Government guarantees the lending bank to the extent
18 of 10 per cent of the aggregate of such loans granted
19 by it prior to December 31st, 1963, but it is up to the
20 bank to set its own standards as to security, credit
21 risks, etc. It is probably because of this latter fact
22 that loans granted under the terms of this Act have not
23 been as numerous as originally expected.

24 7) The recent Throne Speech indicated that the
25 current session of parliament would be asked to increase
26 the size of such loans to \$50,000 and extend eligibility
27 to businesses with an annual gross revenue of \$750,000.
28 This move is strongly endorsed by this Committee.
29 However, it is felt that an increase in the government
30 guarantee to, say, 25 per cent of the aggregate of all



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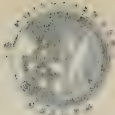
1 such loans granted by a lending bank and an extension
2 of the 1963 deadline would widen the effectiveness of
3 the Act.

4 Public Distribution

5 8) A canvass of a representative group of
6 lending institutions confirmed their reluctance to
7 participate in issues of small businesses. Almost
8 without exception they avoid participation in small stock
9 issues and their investments in small bond issues are
10 very selective and limited. The investment dealer is
11 accustomed to looking to these major pools of money for
12 support in larger issues but the underwriter of smaller
13 issues must rely on the retail buyer. This greatly
14 increases the cost to the issuing company.

15 9) Large investment dealer firms with wide
16 distribution power cannot afford to handle small issues.
17 However, the records show that if the issue has
18 sufficient merit it is probable that an investment
19 dealer can be found to take it on. As previously
20 mentioned 47 I.D.A. members reported handling 217 such
21 issues in the last two years. \$200,000 appears to be
22 the lower limit of practicability for public distribution
23 although smaller issues are occasionally offered.
24 Below this figure the costs are out of proportion and
25 one or more of the major small business problems
26 generally apply. These are

- 27 i. lack of management experience
- 28 ii. lack of management depth
- 29 iii. inability to withstand a recession.
- 30 iv. lack of marketability for the



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- iii. inability to withstand a recession.
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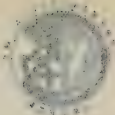
v. reluctance to accept partners on
equal or near equal basis

vi. insufficient amount at risk by the
owner or promoter.

10. The question of marketability is most
difficult and is the objection most frequently cited by
institutions and private investors alike. It strikes
hardest against equity issues for obvious reasons and
applies even in the case of successful operations.

Other Sources of Funds

11. There exist a few public and private
organizations willing to supply funds under certain
conditions. Certain Municipal Industrial Commissions
make funds available to small as well as large businesses
by way of grants of land, commutation of taxes, etc.
In Nova Scotia, the provincial government corporation,
Industrial Estates Limited, will assist in financing
the acquisition of land and buildings. Its existence
has proved helpful on many occasions and has undoubtedly
benefited the province. However, it does nothing to
solve the equity problem. Certain private corporations
are prepared to help with equity but they are ultra
selective and they have only limited funds. It is felt
that in general they are inclined to end up with too
large a share of the common stock. Moreover such
organizations are often unknown to the small management
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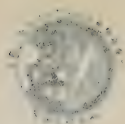
companies are not a source of long term money.



METHODS IN BRITAIN AND THE U.S.

12. The Industrial and Commercial Finance Corporation was set up in 1946 by the Bank of England, the London clearing banks and the Scottish banks, to provide credit for industrial and commercial businesses or enterprises in Great Britain, particularly in cases where the existing facilities provided by banking institutions and underwriters and stock exchanges were not readily or easily available. This Corporation, as in the case of the small business investment companies, was thus intended to supplement but not supersede the activities of other lenders and other financial institutions. The Industrial and Commercial Finance Corporation considers that requirements of credit for small sums (under £ 5,000) can be made by the banks and that larger capital requirements (over £ 200,000) can be satisfied by the new issue market and other credit institutions and the Corporation is precluded from taking up either the whole or part of any loan of more than £200,000. The Corporation's nominal capital was fixed at £15,000,000 and all the shares are to be held by the banks which set up the Corporation which, in addition, may borrow from the shareholding banks up to twice the amount of its capital. It is not permitted to raise money from any other source than from the shareholding banks. It would seem that the shareholding banks in Great Britain now agree that the Industrial and Commercial Finance Corporation has earned itself a permanent place in the monetary system.

13. In the United States the Small Business



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2 1958, has contributed in a very major fashion in
3 providing funds for small business ventures. Congress,
4 after completion of a study by the Federal Reserve
5 which established that long term funds were not easily
6 available, passed a law authorizing the Small Business
7 Administration to license, supervise and, in certain
8 cases, help finance small business investment companies
9 which would serve as sources of equity capital and long
10 term loans to small business. While there have always
11 been individuals and businesses ready to invest in
12 promising situations, the Small Business Administration
13 served to institutionalize the procurement of venture
14 capital for small business and make the rules for
15 such procurement open for public scrutiny, very much as
16 investment dealers and major stock exchanges have done
17 for bigger business both here and in the United States.
18 The success of the program established in the Small
19 Business Administration is indicated by the fact that
20 there are in existence some 425 small business investment
21 companies with capital available for investment in small
22 business amounting to \$500,000,000. In addition to
23 that sum, these small business investment companies may
24 borrow from the S.B.A. 50 per cent of that figure
25 (subject to a limit of \$4,000,000 each). This greatly
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27 borrow from outside sources. It might be noted that
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country. Small business investment companies also enjoy favourable tax advantages commensurate with the development work which they are carrying on.

14, The vast majority of these companies have been successful but some have not. However, sufficient experience has been gained to indicate the weaknesses of the system and this committee feels that a study of the S.B.A. with a view to adapting it to Canadian requirements is warranted.

CONCLUSIONS AND RECOMMENDATIONS

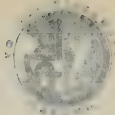
15. (Ia) If a small business has merit and mortgageable assets a persevering and informed management can probably arrange for debt financing through direct mortgage to a lending institutions, the Industrial Development Bank, the Small Business Loans Act or, if not too small, public and occasionally private Placement through an investment dealer.

(Ib) All of these facilities tend to drive companies into borrowing when permanent equity capital may be the proper route for them.

(II) The largest pools of money, the banks and insurance companies, are of little help in long term financing for small businesses even those having mortgageable assets and a long earnings record.

(III) The majority of investment dealers can do little for the business requiring less than \$200,000 and only certain firms will handle anything under \$500,000. Lack of marketability makes public equity financing particularly difficult.

(IV) The low corporation tax rate applicable



country. Small business investment companies also enjoy favourable tax advantages commensurate with the development work which they are carrying on.

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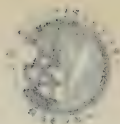


1 to the first \$35,000 of earnings is particularly
2 helpful to small businesses as it enables them to
3 generate more funds internally and also makes them more
4 attractive to potential investors.

5 (V) The operations of the Small Business
6 Administration in the United States are worthy of careful
7 study and consideration should be given to establishing
8 similar legislation here which would result in small
9 business investment companies having similar government
10 support.

11 (VI) Consideration should be given to
12 encouraging the participation of insurance companies,
13 mutual funds and possibly the banks in equity investments
14 in small business investment companies. These large lend-
15 ing investment institutions control tremendous funds
16 practically none of which are at present available either
17 for risk capital or for small business equity
18 investment. If, for example, the life insurance companies
19 were to apply for an amount equal to $1/4$ of 1 per cent
20 of their portfolios to such investments, the proposed
21 small business investment companies would have some \$20
22 million of equity capital for their initial operations.

23 Representatives of certain I.D.A. member
24 firms, with whom this committee consulted, did not
25 agree that these aims should be achieved by legislation.
26 The committee believes that better results could be
27 obtained through encouraging these institutions to
28 attack this problem voluntarily using the methods best
29 suited to their individual circumstances and
30 responsibilities.



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(VII) To encourage public participation in the proposed small business investment companies special tax advantages should be considered. One such could be an increase in the present income tax credit from 20 per cent to 30 per cent for dividends from small business investment companies' shares.

(VIII) Many small entrepreneurs are reluctant to give up much equity. Consideration could be given by appropriate government authority to allow a tax credit, similar to that now made on dividends of Canadian companies, to corporate lenders who may loan money to small businesses or to individual lenders except when they are the owner of the business.



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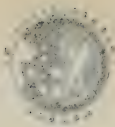
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APPENDIX M

NON-RESIDENT INVESTMENT

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APPENDIX M

NON-RESIDENT INVESTMENT

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Nethercut & Young

Toronto, Ontario

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4 and Municipal Securities in
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6 1961).
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and A.680

Canadian Securities (1956-61)

and Municipal Securities in
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1961)

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1 Introduction

2 1. The following brief outlines the role
3 of non-resident investment in Canada, with particular
4 emphasis on fixed monetary claims represented by
5 debt. The factors which determine the composition
6 and extent of purchases of debt securities by non-
7 residents are outlined below:

8 General

9 2. Periods of great economic expansion in
10 Canada have, in the past, brought foreign capital to
11 this country. The most recent period of expansion,
12 namely between 1946 - 1960, is the one we are particularly
13 interested in, and is by far the greatest. Gross national
14 product rose from \$11,850,000,000 in 1946 to
15 \$34,857,000,000 in 1959. Foreign long term investment
16 in Canada rose from \$7.1 billion in 1945 to \$20.6
17 billion in 1959.

18 3. While in earlier periods of expansion,
19 capital came mostly from England and France, the United
20 States has recently been by far the largest supplier
21 of capital. In 1959 the total value of United States
22 investments in Canada was divided as follows:

23 Direct Investment	\$ 9,850 million
24 Government and Municipal	2,767 million
25 Other Portfolio	2,238 million
26 Miscellaneous	<u>870 million</u>
27	\$15,725 million

28 This compares with the total of
29 \$20.6 billion from all countries.

30 4. The growth of gross national product,



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1 gross capital formation and the extent to which this
2 was financed from domestic and foreign resources is
3 shown in Exhibit 1, appended hereto.

4 5. From 1946 to 1949 Canada raised at home
5 sufficient capital to finance its gross capital form-
6 ation and, in fact, was a net exporter of capital. In
7 the subsequent years, foreign capital was imported in
8 extremely large amounts and in 1959 over 29 per cent
9 of the gross capital formation was financed by the use
10 of foreign resources. In 1960 and 1961 this capital
11 inflow was substantially reduced.

12 6. Foreign capital has come to Canada in
13 two main forms:

14 (a) Direct Investment

15 (b) Security or Portfolio Investment

16 Direct Investment

17 7. Direct investment involves the establish-
18 ment of branch manufacturing plants by foreign companies,
19 foreign purchase of established companies, direct
20 foreign development of natural resources and construction
21 of buildings of all kinds, etc. This particular kind
22 of investment is almost entirely outside the field of
23 the investment dealer but the amount of new capital
24 invested in Canada in this way accounts for approximately
25 two-thirds of all foreign investments. In many instances
26 this capital has been accompanied by new techniques
27 and has, consequently, developed resources in Canada
28 that otherwise would never have been developed.

29 8. At the same time, direct foreign control
30 has caused problems for Canada, particularly in the area



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1 of secondary manufacturing.

2 9. Canadian commercial policy has historically
3 manifested itself in tariffs designed to provide a
4 measure of protection for secondary manufacturing.
5 This protection has encouraged United States companies
6 to "jump" Canadian tariff walls and establish branch
7 plant operations in Canada. In recent years, Canadian
8 manufacturing has suffered from a large number of small
9 firms operating in a limited market, resulting in excess
10 capacity and high unit costs.

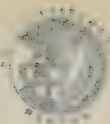
11 10. Exhibit 2 shows the amount of direct
12 investment each year from 1946 to 1961.

13 Security or Portfolio Investments

14 11. The extent of sales of Canadian securities
15 to non-residents is shown in Exhibit 2, and Exhibit 4.

16 12. The flow of capital to Canada through
17 security or portfolio investments did not just happen.
18 The investment dealer, with his knowledge of the huge
19 demand for capital went out to foreign countries and
20 sold investment opportunities in Canada to foreigners.
21 Branches were established in foreign countries, mainly
22 New York City and London, England and dealers directly
23 contacted foreign institutional accounts. The investment
24 dealer was so successful in selling Canada that Canadian
25 portfolio securities became an established medium of
26 investment.

27 13. The extent to which Canada benefited from
28 this inflow of capital can be visualized to some degree
29 by reviewing some of the major projects that were, at
30 least partly, made possible by these funds:



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(a) the construction of all the large pipelines, including gathering systems, to transport oil and gas from the mid-western fields to the eastern and Pacific markets,

(b) the development of iron mines in Quebec and Labrador and the construction of railroads into these areas,

(c) the Kitimat development of the Aluminum Co. of Canada,

(d) the huge hydro projects in most of the Provinces, but particularly those in Ontario and Quebec,

(e) construction of schools, hospitals, roads and subways by the major cities in Canada.

14. The investment dealers performed an important function in financing these developments by selling securities to non-residents when this capital was required.

15. External sales of new issues by Provincial, Municipal and Corporate debt securities in the period 1956 - 1960 amounted to \$2,861,000,000.

Type of Security Sold in the United States

16. There are three main types of securities sold in the United States:

(a) United States payment bonds and debentures of Provinces, Municipalities and Corporations,

(b) Canadian payment bonds and debentures,



1 (c) Stocks.

2 United States Payment Bonds and Debentures.

3 17. The type of security sold in the United
4 States that produced the main source of capital funds
5 was United States payment debt securities created for
6 that market. Between 1954 and 1959 United States
7 investors increased their holdings of Canadian debt
8 securities, payable externally, by \$1,469,000,000 as
9 compared to \$301 million in securities payable in
10 Canadian funds only. In addition to being payable in
11 the United States these securities were free from all
12 Canadian taxes. In most instances they were made legal
13 for investment of insurance companies and other
14 institutions, were rated by the various statistical
15 services and were issued for a term and with callable
16 features attractive to the market. The yield return
17 was also favourable in relation to comparable securities
18 issued in the foreign market.

19 Canada Payment Securities

20 18. These securities were issued mainly for
21 the Canadian market but were purchased by non-residents
22 when the Canadian market and the exchange rate made the
23 yield return particularly attractive. Canadian payment
24 bonds and debentures are not nearly as acceptable in
25 the United States as securities payable in that
26 country. Many institutions are unable to buy them under
27 the laws of the various states and in addition, the
28 buyer is required to take an exchange risk which he
29 would ordinarily avoid.

30 19. Canadian Government and Guaranteed bonds



(c) Stocks.

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1 of Canada were, until 1960 the only internal bonds
2 free from Canadian withholding taxes and these
3 securities were at times purchased extensively by non-
4 residents.

5 Stocks

6 20. Although the sales of stocks to foreign
7 countries are included in our tables as part of the
8 trade with non-residents, Appendix J deals with this
9 subject.

10 Main Purchasers of Securities in the United States

11 21. The main purchasers of Canadian debt
12 securities in recent years are:

13 Life Insurance Companies

14 Pension Funds - both government and industrial

15 Savings Banks

16 Trust Departments of Banks

17 Charitable and Educational Funds

18 22. All non-resident insurance companies that
19 write insurance in Canada are required to maintain in
20 Canada a deposit of securities equal to their liabilities
21 in Canada. Investment dealers, in many cases, sell
22 securities to these companies for this purpose by direct
23 calls to the Head Office of the company in the United
24 States. The volume of securities sold for this purpose
25 is substantial but in practically all instances, the
26 actual money invested is generated by these companies
27 in Canada and is part of the total savings of Canadians
28 and does not affect our balance of payments position.
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1 Comments on the Importance of Certain Factors on the
2 Trade in Canadian Securities with Foreigners

3 Exchange Rates

4 23. The yearly high and low value of the
5 United States dollar in Canada between 1951 and 1961
6 is shown in Exhibit 3.

7 24. The greatest flow of capital to Canada
8 took place when the Canadian dollar was at a substantial
9 premium. This would appear to indicate that the exchange
10 value of the Canadian dollar was mainly the result
11 rather than the cause of the capital flow.

12 25. In 1950 and early 1951 the United
13 States dollar was at a fixed premium of approximately
14 10 per cent. At that time there was a good deal of
15 speculation that the Canadian dollar would advance
16 in price and foreigners bought large quantities of
17 Canadian securities. The change to a free rate in 1951
18 was definitely influenced by the capital movement.

19 26. In June 1961, the Government announced
20 its intention of taking action to move the value of
21 the Canadian dollar to its "appropriate" level. The
22 value of the Canadian dollar immediately started to
23 decline and recently has fluctuated between a 3 - 5
24 per cent discount.

25 Relative Yields

26 27. In the attached Exhibit 3, we show the
27 spread in yield which exists between a particular
28 Canadian Government security in Canada and a
29 comparable United States Government security in the
30 United States. Yields on Canadian long term Government



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UNITED STATES GOVERNMENT
BUREAU OF THE PUBLIC DEBT

Relative Yields

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2 States issues from 1950 onward. As a result, Canadian
3 issuers were able to sell securities payable in United
4 States funds in the United States at yield rates which
5 appeared to be more attractive than comparable rates in
6 Canada. In fact, this condition exists today but mainly
7 because of Government persuasion, Canadian issuers are
8 confining their offerings to the Canadian market. (See
9 Exhibit 5).

10 28. It is interesting to note as well that
11 since 1950, the year 1955 was the only year in which
12 Canada actually repatriated more of its securities
13 abroad than it sold abroad and this was the year in which
14 the spread in yield in favour of Canadian securities
15 got to a relatively low level.

16 29. It should also be pointed out that yields
17 on debt securities were probably lower in Canada
18 between 1950 and 1959 than they would have ordinarily
19 been because of the large volume of security sales in
20 the United States.

21 Legislation and Tax Factors

22 Legislation in the Foreign Country

23 30. It is only in recent years that various
24 States in the United States have made certain Canadian
25 securities legal for the investment of insurance
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Legislation and Tax Factors

Legislation in the Foreign Country

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1 Legislation in Canada

2 31. In the period from 1951 to 1959 Canadian
3 laws favoured foreign investors. External payment
4 Canadian bonds and Canadian Government internal bonds
5 were free of all Canadian withholding taxes.

6 32. In late 1960 and subsequently, certain
7 actions were taken pertaining to Government policy that
8 curtailed foreign sales of securities.

9 33. These included:

10 (a) The suggestion by inference in the
11 budget speech of December 1960 that
12 Canadian borrowers finance their
13 requirements in Canada,

14 (b) The exemption from Canadian with-
15 holding taxes was withdrawn from external
16 payment and Canadian government internal
17 bonds, issued after December, 1960,

18 (c) The Government policy to reduce the
19 foreign exchange value of the Canadian
20 dollar.

21 34. Some other events that caused uneasiness
22 amongst foreign investors and indirectly reduced sales
23 were:

24 (a) Federal Budgetary deficits,

25 (b) Controversy over the Governor of
the Bank of Canada,

26 (c) The manner in which the British
27 Columbia Electric Company was
28 acquired by the Province of
British Columbia.

29 35. The Government suggestion that Canadian
30 borrowers finance their requirements in Canada was



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1 particularly effective in reducing sales because since
2 that time there have been practically no new issues of
3 foreign payment bonds sold by the Provinces of
4 Municipalities.

5 36. The imposition of the withholding tax
6 on external payment bonds could be having, and will have,
7 a great effect on the volume of sales to non-residents.
8 Among the largest buyers by volume of the highest grade
9 external payment bonds in the past have been government
10 and industrial pension funds, savings banks and fraternal
11 organizations. These institutions pay little or no tax
12 in their own country but they are not exempt from the
13 Canadian withholding tax. The burden of this with-
14 holding tax would reduce substantially the yield return
15 on new issues of Canadian securities and, as a consequence,
16 these institutions are no longer buyers of Canadian
17 securities that are subject to this tax.

18 37. It is probably too early for statistics
19 to show the long term effect that these factors will
20 have on foreign investment but net sales of securities
21 were substantially reduced in 1960 and 1961. In
22 addition, there was a marked change in the category
23 of investment. Foreign direct investment in Canada
24 produced substantially more capital than net sales of
25 securities. In the period 1956 to 1959 the opposite
26 was the case.

27 Conclusion

28 38. In the years of great expansion in Canada
29 when the savings of the country were insufficient to
30 provide the necessary capital and Canadian industry



institutions.

36. The imposition of the withholding tax

on external payment bonds could be having, and will have, a great effect on the volume of sales to non-residents. Among the largest buyers by volume of the highest grade external payment bonds in the past have been government and industrial pension funds, savings banks and fraternal organizations. These institutions pay little or no tax in their own country but they are not exempt from the Canadian withholding tax. The burden of this withholding tax would reduce substantially the yield return on new issues of Canadian securities and, as a consequence, these institutions are no longer buyers of Canadian securities that are subject to this tax.

37. It is probably too early for statistics

to show the long term effect that these factors will have on foreign investment but net sales of securities were substantially reduced in 1960 and 1961. In addition, there was a marked change in the category of investment. Foreign direct investment in Canada produced substantially more capital than net sales of securities. In the period 1956 to 1959 the opposite was the case.

Conclusion

38. In the years of great expansion in Canada



1 the capital goods, the investment industry went outside
2 the country and sold securities to foreigners. It
3 was shown that Canada had a good climate for foreign
4 investment because of the character of the people, the
5 sound Government policies and generally favourable
6 economic conditions which indicated substantial growth.

7 39. As a result, foreign legislative bodies
8 approved of and institutions accepted Canadian securities
9 that were designed for the various markets and indicated
10 their willingness to buy on a continuing basis. There
11 is no doubt that the funds provided, increased the
12 standard of living and wealth and the continuance
13 of a flow of funds to Canada for productive purposes
14 would undoubtedly create more wealth.

15 40. In the last two years at least, partly
16 because of government legislation and action, the net
17 inflow of foreign capital has been reduced. Neverthe-
18 less, the post-war trend of an increase in the relative
19 importance of equity as against debt, reflecting the
20 increase of direct investment has been intensified,
21 carrying with it greater foreign ownership and control
22 of Canadian business.

23 41. We are in accord with the policy that
24 Canada should use its domestic resources to finance
25 capital formation by using its own plant and labour to
26 the utmost, providing at the same time, the standard
27 of living of the population is being increased to the
28 greatest extent possible.

29 42. As long as Canada continues to have a
30 deficit of international payments on current account,



the capital goods, the investment industry went outside the country and sold securities to foreigners. It was shown that Canada had a good climate for foreign investment because of the character of the people, the sound government policies and generally favourable economic conditions which indicated substantial growth. 39. As a result, foreign legislative bodies

approved of and institutions accepted Canadian securities that were designed for the various markets and indicated their willingness to buy on a continuing basis. There is no doubt that the funds provided, increased the standard of living and wealth and the continuance of a high level of living and wealth and the continuance of a high level of living and wealth.

40. In the last two years at least, partly because of government legislation and action, there has been a reduction in the flow of foreign capital has been reduced. Nevertheless, the post-war trend of an increase in the relative importance of equity as against debt, reflecting the increase of direct investment has been intensified, carrying with it greater foreign ownership and control of Canadian business.

41. We are in accord with the policy that Canada should use its domestic resources to finance capital formation by using its own plant and labour to the utmost, providing at the same time, the standard of living of the population is being increased to the

42. As long as Canada continues to have a deficit of international payments in current account,



1 funds must be provided from foreign sources.

2 Recommendations

3 43. Financial policy in Canada should be
4 directed towards the following:

5 To the extent that it is
6 necessary or desirable to import
7 capital from foreign countries,
8 Government policy should be such
9 that it favours the purchase by
10 foreigners of debt securities rather
11 than equity investments of all kinds.

12 44. If effectively pursued, such policies
13 would contribute to an increasing Canadian participation
14 in our economic development and to a growing ownership
15 of this nation's industry and resources.



capital from foreign countries,

foreigners of debt securities rather

- 8 -

GROSS NATIONAL PRODUCT
and
USE OF DOMESTIC AND FOREIGN RESOURCES
in
GROSS CAPITAL FORMATION IN CANADA

Year	G.N.P. at Market Prices	Gross Capital Formation	% of G.N.P.	Net Use of Domestic Resources	Net Use of Foreign Resources	Foreign Resources as % of Gross Capital Formation
(Dollar amounts expressed in billions)						
1946	\$ 11.85	\$ 2.0	16.9%	\$ 2.2	\$ -.2	- %
1947	13.17	2.8	21.3	2.6	.2	7.1
1948	15.12	3.2	21.2	3.3	-.1	-
1949	16.34	3.6	22.0	3.5	.1	2.8
1950	18.01	4.5	25.0	3.8	.6	13.3
1951	21.17	5.7	26.9	4.8	.9	15.8
1952	24.00	6.0	25.0	5.6	.4	6.7
1953	25.02	6.6	26.4	5.4	1.2	18.2
1954	24.87	5.6	22.5	4.4	1.2	21.4
1955	27.13	6.6	24.3	4.9	1.7	25.8
1956	30.59	9.1	29.7	6.7	2.4	26.4
1957	31.91	8.9	27.9	6.3	2.6	29.2
1958	32.87	8.0	24.3	6.0	2.0	25.0
1959	34.86	8.7	25.0	6.2	2.6	29.9
1960	35.96	8.5 p	23.6	6.3	2.2 p	25.9

p - preliminary

Source: - Dominion Bureau of Statistics: 67-201

Population Census of Canada
as at June 1st

1951	14,009,429
1956	16,080,791
1961	18,238,247

* * * * *

Exhibit 2SELECTED NON-RESIDENT CAPITAL TRANSACTIONS
and

CURRENT ACCOUNT BALANCES FOR CANADA

1946 - 1961

<u>Year</u>	<u>Canadian Current Account Balance of International Payments (1)</u>	<u>Foreign Direct Investment in Canada</u>	<u>Net New Issues of Canadian Securities</u>	<u>Net Increase in Foreign Holdings of Canadian Portfolio Securities</u>	<u>As % of Net New Issues</u>
(millions of dollars)					
1946	+ 363	40	28	- 127	--
1947	+ 49	61	- 84	- 282	--
1948	+ 451	71	168	39	23.2
1949	+ 177	94	64	- 34	--
1950	- 334	222	388	255	65.7
1951	- 517	309	157	265	168.8
1952	+ 164	346	976	133	13.6
1953	- 443	426	983	158	16.1
1954	- 432	392	972	191	19.7
1955	- 698	417	1849	- 45	--
1956	- 1366	583	1588	725	45.7
1957	- 1455	514	2279	757	33.2
1958	- 1131	420	3048	607	19.9
1959	- 1504	550	2281	650	28.5
1960	- 1217 p	645 p	1964	246	12.5
1961	- 989 p	420 p		303	

Notes: (1) + indicates surplus
- indicates deficit

(2) See Exhibit 4 for detailed account of transactions for years 1956 to 1961.

p preliminary

Sources: Dominion Bureau of Statistics 67-201
Bank of Canada Statistical Summary

COMPARISON OF YIELDS
ON
SELECTED CANADIAN AND UNITED STATES GOVERNMENT SECURITIES
IN CURRENCY OF PAYMENT

	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>
Govt. of Canada <u>2 3/4% Jan. 15, 1967/68 (1)</u>											
(a) High	3.48	3.63	3.63	3.59	3.42	4.01	4.81	4.52	5.37	5.55	4.75
Low	2.98	3.47	3.47	2.92	2.81	3.24	3.66	3.31	4.45	4.09	4.12
U. S. Govt. <u>2 1/2% Dec. 15, 1963/68</u>											
(a) High	2.71	2.73	2.73	2.66	2.98	3.49	3.93	3.94	4.90	4.97	4.20
Low	2.31	2.53	2.53	2.33	2.60	2.78	2.99	2.66	3.80	3.46	3.53
Yield Spread in Favour of Canadian Issue											
(b) Maximum Spread	.57	1.03	1.01	.99	.58	.66	1.06	.87	.99	1.13	1.18
Minimum Spread	.44	.76	.58	.40	.01	.35	.33	- .09 (2)	.34	.23	.07
Govt. of Canada <u>3 1/4% Oct. 1, 1979 (1)</u>											
(a) High				3.26	3.44	3.90	4.35	4.42	5.30	5.42	5.28
Low				3.22	3.13	3.30	3.79	3.78	4.41	4.63	4.77
U. S. Govt. <u>3 1/4% June 15, 1978/83</u>											
(a) High				2.93	3.01	3.39	3.71	3.88	4.41	4.48	4.11
Low				2.58	2.71	2.88	3.22	3.06	3.84	3.70	3.70

- continued

Exhibit 2 - continued

	<u>1951</u>	<u>1952</u>	<u>1953</u>	<u>1954</u>	<u>1955</u>	<u>1956</u>	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>
Yield Spread in Favour of Canadian Issue											
(b) Maximum Spread				.61	.57	.59	.94	.79	1.20	1.39	1.41
(b) Minimum Spread				.56	.22	.36	.36	.25	.50	.87	.73

Exchange Value of U.S. Dollar in Cdn. Currency											
High	7 5/16P	1 1/3P	7/32D	1 1/4D	1 1/16P	1 1/32D	1 3/8D	27/32D	1 13/16D	3/16D	4 3/8P
Low	1 3/16P	4 1/8D	3 1/8D	3 21/32D	3 17/32D	4 11/32D	5 25/32D	4 1/4D	5 7/16D	5 1/16D	1 3/4D

Notes: (1) Payable in Canadian currency

(2) On September 3rd, Cda's. 2 3/4/68 yielded 3.59% as against 3.68% for U. S. 2 1/2/68

Source:

Compiled by the Investment Dealers' Association of Canada from figures extracted from Bank of Canada Statistical Summary.

(a) Figures shown for years 1951-53 are from closing mid-market quotes for the middle Wednesday of each month, from which quotes the above highs and lows have been taken. Figures for 1954 and subsequent years are compiled from closing mid-market quotes each Wednesday of the year.

(b) The figures for yield spreads are calculated from the same sources as were used in (a) but represent the maximum and minimum spread in yield between the prices quoted for the two securities on any given Wednesday, without reference to the high or low points in actual yields.

* * * * *

Exhibit 4

- 12 -

NON-RESIDENT TRANSACTIONS IN CANADIAN SECURITIES

1956 - 1961

Year	Category (1)	Net Transactions in Outstanding Securities	Sales of New Issues to Non-Residents	Retirements of Foreign-Held Securities	Net Capital Inflow from Transactions
(\$ m i l l i o n s)					
<u>1956</u>	Government	6	9	83	- 68
	Provincial	- 11	224	15	198
	Municipal	2	112	18	96
	Corporate	<u>14</u>	<u>252</u>	<u>20</u>	<u>246</u>
	Total Bonds	11	597	136	472
	Stocks	<u>188</u>	<u>70</u>	<u>5</u>	<u>253</u>
	Total Securities	199	667	141	725
<u>1957</u>	Government	- 14	16	29	- 27
	Provincial	- 15	136	25	96
	Municipal	- 1	123	24	98
	Corporate	- <u>15</u>	<u>462</u>	<u>30</u>	<u>417</u>
	Total Bonds	- 45	737	108	584
	Stocks	<u>137</u>	<u>61</u>	<u>25</u>	<u>173</u>
	Total Securities	92	798	133	757
<u>1958</u>	Government	20	76	25	71
	Provincial	- 18	168	45	105
	Municipal	- 1	148	30	117
	Corporate	- <u>1</u>	<u>242</u>	<u>42</u>	<u>199</u>
	Total Bonds	-0-	634	142	492
	Stocks	<u>88</u>	<u>43</u>	<u>16</u>	<u>115</u>
	Total Securities	88	677	158	607
<u>1959</u>	Government	118	56	101	73
	Provincial	- 5	334	41	288
	Municipal	2	158	34	126
	Corporate	- <u>24</u>	<u>112</u>	<u>65</u>	<u>23</u>
	Total Bonds	91	660	241	510
	Stocks	<u>110</u>	<u>47</u>	<u>17</u>	<u>140</u>
	Total Securities	201	707	258	650
<u>1960</u>	Government	49	31	58	22
	Provincial	- 8	102	51	43
	Municipal	4	135	35	104
	Corporate	- <u>42</u>	<u>153</u>	<u>100</u>	<u>11</u>
	Total Bonds	3	421	244	180
	Stocks	<u>49</u>	<u>26</u>	<u>9</u>	<u>66</u>
	Total Securities	52	447	253	246

STATE OF NEW YORK
DEPARTMENT OF TAXATION
1917

Year	Category (1)	Transactions in Outstanding Securities	Sales of New Issues to Non-Residents	Retirements of Securities Issued	Net Change
1916	Government	11	297	83	11
	Provincial	- 11	294	18	18
	Municipal	- 11	118	18	18
	Corporate	14	223	20	20
	Total Bonds	11	927	129	11
	Stocks	193	70	-	193
	Total Securities	193	657	129	758
1917	Government	- 14	16	-	16
	Provincial	- 14	16	-	16
	Municipal	- 1	123	-	123
	Corporate	- 12	443	-	443
	Total Bonds	- 45	737	-	737
	Stocks	193	64	-	193
	Total Securities	92	798	129	758
1918	Government	20	76	-	20
	Provincial	- 18	166	-	166
	Municipal	- 1	148	-	148
	Corporate	- 1	243	-	243
	Total Bonds	- 0	633	-	633
	Stocks	83	43	-	83
	Total Securities	83	677	-	677
1919	Government	118	56	-	118
	Provincial	- 2	334	-	334
	Municipal	- 2	158	-	158
	Corporate	- 24	143	-	143
	Total Bonds	91	689	-	689
	Stocks	110	17	-	110
	Total Securities	201	707	-	707
1920	Government	27	21	-	27
	Provincial	- 2	443	-	443
	Municipal	- 2	143	-	143
	Corporate	- 1	123	-	123
	Total Bonds	22	707	-	707
	Stocks	45	17	-	45
	Total Securities	67	724	-	724

- M -

- 13 -

Exhibit 4 - continued

<u>Year</u>	<u>Category (1)</u>	<u>Net Transactions in Outstanding Securities</u>	<u>Sales of New Issues to Non-Residents</u>	<u>Retirements of Foreign-Held Securities</u>	<u>Net Capital Inflow from Transaction</u>
(\$ m i l l i o n s)					
<u>1961</u>	Government	75	37	47	65
	Provincial	- 8	53	23	22
	Municipal	3	36	40	- 1
	Corporate	- 7	<u>330</u>	<u>129</u>	<u>194</u>
	Total Bonds	63	456	239	280
	Stocks	<u>40</u>	<u>36</u>	<u>53</u>	<u>23</u>
	Total Securities	103	492	292	303

Notes: (1) Bonds and Debentures include direct and guaranteed issues in each category

Source: Dominion Bureau of Statistics 67-201 and 67-002

* * * * *

Category (1)	Transactions in Outstanding Securities	Sales of New Issues in Outstanding Securities	Outstanding in Outstanding Securities	Category (2)
(\$ millions)				
Government	72	37	63	Government
Provincial	- 8	33	21	Provincial
Municipal	3	36	25	Municipal
Corporate	- 2	330	252	Corporate
Total (Total)	63	436	361	Total (Total)
Stocks	10	3	13	Stocks
Total Securities	103	462	394	Total Securities

(1) Bonds and Debentures include direct and guaranteed issues in each category

Domestic Bureau of Statistics 67-201 and 67-002

QUOTATIONS ON CANADIAN PROVINCIAL AND MUNICIPAL SECURITIES
IN CANADA AND THE UNITED STATES
(March 12th, 1962)

Market Quotations in United States on Securities Payable in United States Funds		Market Quotations in Canada on Securities Payable in Canadian Funds	
Price	Yield	Price	Yield
Province of Ontario 4 3/4% Bonds Due 1st February 1984	102 1/2	Province of Ontario 5 1/4% Bonds Due 15th March 1982	100 3/8
Quebec Hydro-Electric Comm. 5% Bonds Due 15th July 1984	105 1/2	Province of Quebec 5 1/4% Bonds Due 1st April 1984	99 5/8
Metropolitan Toronto 5% Bonds Due 1st June 1979	105	Metropolitan Toronto 5 1/2% Bonds Due 15th February 1982	101 1/2

United States Funds quoted in Canadian dollars
@ 4 7/8% -- 4 15/16% Premium

* Issued prior to December 1960

ESTIMATES (API) WITH THE LATEST INFORMATION AVAILABLE TO THE SECRETARY OF THE ARMY AND NAVY (1961, 1962, 1963)

Changes in expenditures for
at various points in
the year

Estimated expenditures for
the year in various points in
the year

1961

1961

1961

1

1961

1961

1961

1961

1961

1961

1961

1961

1961

Estimated expenditures for
the year in various points in
the year

Estimated expenditures for
the year in various points in
the year



APPENDIX N

TAXATION

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Comparison of Canada's Tax System to Other Countries	A.696
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ANNEX II
TAXATION

Contents

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A.696	A More Equitable Distribution of Taxes
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A.693	The Need for a Comprehensive Study of the Taxation Studies Currently in Progress
A.692	Basic Principles and Areas for Examination
A.691	Introduction



The Taxation Portion of the Brief
submitted by The Investment Dealers'
Association of Canada

Introduction

1. In a complex and industrialized economy such as we have in Canada, taxes are recognized as a major factor and instrument of economic policy. To indicate the importance of taxes, government revenue at all levels for 1960 represented approximately 28.7 per cent of Canada's gross national product, and of this, taxes provided about 82 per cent (See Exhibit A).

2. Government taxing and spending now occupies a prominent position on the economic landscape for a variety of reasons, and expenditures by governments at all levels have increased very greatly compared to the pre World War II era, most of such increase having taken place during a period of unprecedented economic expansion. Such spending, perhaps some of which has been made for reasons hinging more on political expediency than on actual need, has had to be financed by increased revenues. To be more specific, in 1939 government revenue at all levels represented approximately 20 per cent of Canada's gross national product in such year, compared to the present level of about 29 per cent. On a percentage basis this is an increase of nearly 50 per cent. Furthermore, this percentage increase relates to a very greatly increased gross national product. On a dollar basis the increase is very much greater, the total revenue for 1939 by governments at all levels being approximately \$1,110,000,000, compared to the figure for 1960 of

Introduction

1. In a complex and industrialized economy such as we have in Canada, taxes are recognized as a major factor and instrument of economic policy. To illustrate the importance of taxes, the following figures at all levels for 1960 represented approximately 88.7 per cent of Canada's gross national product, and of this, taxes provided about 82 per cent (See Exhibit A).

2. Government taxing and spending now occupies a prominent position on the economic landscape for a variety of reasons, and expenditures by governments at all levels have increased very greatly compared to the pre World War II era, most of such increase having taken place during a period of un-
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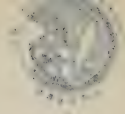


1 \$10,306,000,000. In other words, on a dollar basis, the
2 present requirement by governments at all levels is
3 nearly ten times that of 1939. Expressed on a per
4 capita basis, total revenue for 1939 by government
5 at all levels averaged approximately \$95 per person for
6 the population in such year, but by 1960 this had risen
7 to a figure of \$560 per person; an increase of nearly
8 500 per cent. In all years studied, taxes provided in
9 excess of 80 per cent of government revenue (See Exhibit
10 A). Only by a reduction in government spending can
11 taxes, the principal source of government revenue, be
12 realistically and permanently reduced.

13 3. It is against this background of increased
14 government spending and the present means of financing
15 this spending, relying as it does largely upon our
16 taxation structure, that we believe the tax policies
17 currently existing in Canada must be critically examined.

18 4. The growth of an economy depends on an
19 increasing demand for goods produced and services
20 rendered. The willingness of consumers, businesses and
21 governments to spend money for goods and services, leads
22 to utilization of capacity or expansion of such capacity.
23 Conversely, lack of spending leads, not only to reduced
24 utilization of capacity, but to unemployment of
25 individuals. This in turn fosters the trend towards
26 state socialism, requiring greater expenditure by
27 government for purposes that may tend to be unproductive.

28 5. To adjust for the fluctuations caused by
29 either over-utilization or under-utilization of capacity,
30 present day economic thinking seems to have accepted the



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either over-utilization or under-utilization of capacity.
5. To adjust for the fluctuations caused by
Government for purposes that may tend to be unproductive.
Some economic experts believe that
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A). Only by a reduction in Government spending can
excess of 80 per cent of Government revenue (See Exhibit
500 per cent. In all years studied, taxes provided in
to a figure of \$260 per person; an increase of nearly
the population in such year, but by 1960 this had risen
at all levels averaged approximately \$95 per person for
capita basis, total revenue for 1959 by Government
nearly ten times that of 1939. Expressed on a per
present requirement by Governments at all levels is
\$1,000,000,000. In other words, on a dollar basis, the



1 principle that governments, either directly or through
2 controlled indirect operations (such as a Central Bank)
3 should endeavour to alleviate such fluctuations. In an
4 attempt to mildly suppress the economy during boom
5 period, spending is discouraged by government, and to
6 strengthen the economy during recession periods, spending
7 is encouraged. We consider it desirable that
8 governments, with moderation, use periods of economic
9 expansion to reduce debt and generally strengthen the
10 economic framework of the country in preparation for
11 periods of recession, when deficit and debt financing
12 may become necessary.

13 6. Today, the heavy tax "load", and the
14 method of application of such taxes, is having a profound
15 effect on our economy, and the appeal being heard from
16 many sources (see Exhibit B) for a thorough examination
17 of Canada's taxation system is most appropriate. It
18 is particularly so in relation to the problem of using
19 fiscal policy as an aid in regulating the severity of
20 business cycles. It is even possible that, of the
21 various alternatives open to government to raise money
22 now required for public spending, a tax levied upon
23 income, as opposed to other means of producing revenue,
24 may be a less than satisfactory method and in many
25 respects may be undesirable.

26 Basic Principles and Areas for Examination

27 7. Without restricting the area of study of
28 our taxation system, we wish to express an opinion on
29 some of the basic principles that need to be examined
30 in any major tax study. These basic principles and the





1 areas in need of study are as follows:

- 2 1. A general simplification of the
- 3 total taxation system which would
- 4 result in a greater understanding
- 5 of its operation along with increased
- 6 ease of collection.
- 7 ii. A more equitable distribution of
- 8 the tax load than is currently the case.
- 9 iii. Increasing use of indirect taxation
- 10 in order to broaden the tax base.
- 11 iv. Greater use of the incentive approach
- 12 in order to direct economic activity
- 13 and individual endeavour, and to funnel
- 14 savings into revenue and employment
- 15 producing activities.
- 16 v. An examination and study of the
- 17 taxation systems and practices of certain
- 18 other countries that are experiencing
- 19 problems similar to those currently
- 20 being experienced in Canada in order
- 21 to see how such problems have been met
- 22 by other countries.
- 23 vi. A detailed study of the problems
- 24 currently relating to various types
- 25 of corporate surplus.
- 26 vii. The effects of double taxation,
- 27 particularly as it relates to corporate
- 28 dividends.
- 29 viii. The effect of the current tax
- 30 structure on the types of financing



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1 being carried out by Canadian corporations.

2 ix. Examination of the division between
3 capital gains and income in order to
4 define and differentiate more clearly
5 between the two.

6 x. The ability of a taxpayer to obtain
7 a tax ruling prior to a transaction,
8 as is possible in other countries.

9 xi. The elimination of the current tax
10 disadvantages to Canadian individuals
11 in the development of oil and other
12 natural resources as compared to the
13 position of individuals in the United
14 States operating in Canada.

15 xii. Finally, it is important that a
16 tax system be evolved to encourage,
17 as much as possible, the orderly
18 development and expansion of the Canadian
19 economy for the benefit of all Canadians.

20 Taxation Studies Currently in Progress

21 8. We fully appreciate the long and arduous
22 task involved in any major study of the existing
23 Canadian tax structure and for this reason we believe
24 that those undertaking any such study should avail
25 themselves of prior studies on taxation in Canada.

26 9. At the present time Queen's University,
27 Kingston, sponsored by the Canadian Tax Foundation, is
28 in the process of carrying out a study of the level and
29 structure of taxation in Canada, emphasizing the effects
30 of changes in taxation on the economic growth of Canada.



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1 This study is to be completed not later than September
2 30, 1964.

3 10. The scope of the Queen's University study
4 is extremely broad and encompasses many, although by no
5 means all, of the areas that we believe should be
6 examined, and we suggest that the results of this
7 particular study on taxation should be carefully
8 considered.

9 The Need for a Comprehensive Study of the Canadian
10 Tax Structure

11 11. It is our opinion that a complete
12 investigation of the working of the Canadian tax
13 structure today is essential in order to provide the
14 proper emphasis on the direction in which the Canadian
15 economy should be moving in a world environment which is
16 now so different to that which existed prior to World
17 War II. To indicate this change, at the present time
18 approximately 56 per cent of Canadian exports (by
19 dollar volume) are now being made to the United States
20 as compared to only about 33 per cent prior to World War
21 II. In this same period exports to Great Britain
22 declined to approximately 17 per cent from over 40 per
23 cent of the total (see Exhibit C). These fundamental
24 and basic changes would in themselves, we believe,
25 warrant a detailed investigation of the present Canadian
26 tax system.

27 12. In addition, recognition of the trend
28 towards the formation of large economic blocks is of
29 equal importance in judging the suitability of Canada's
30 present tax structure. The United States represents one



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approximately 10 per cent of Canadian exports (in dollar volume) are now being made to the United States as compared to only about 33 per cent prior to World War

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1 of these major blocks and, as a result of its proximity,
2 its influence has been one of the major factors affect-
3 ing the direction in which the Canadian economy has tend-
4 ed to move over the years. This influence may not
5 be in the best long term interests of Canada. More
6 recently the formation of the European Common Market
7 represents the creation of another major block and,
8 within a short period of time, the consolidation and
9 forward momentum of this block may well affect Canada's
10 exports to the countries forming this block.

11 13. In view of the above changes that have
12 taken place and the possibility of greater changes in
13 the near future, and as the present Canadian tax
14 structure was formulated under conditions very different
15 to those existing today, we respectfully submit that a
16 thorough review of the Canadian tax structure is long
17 overdue and is essential for continued Canadian
18 prosperity.

19 General Comments and Factors Meriting Examination
20 Simplification of the Tax System

21 14. In our discussions with various tax
22 authorities we have encountered the apparently general
23 opinion that the Canadian tax structure, as it now
24 stands, does not compare too unfavourably with the
25 tax structures of other major industrialized countries
26 with regard to simplicity and fairness to the individual.
27 Nevertheless, in view of Canada's position in the world
28 today, such a fact we believe does not state the case
29 adequately and, in our opinion, taxes in Canada are
30 high and not always easy to determine.

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RECOMMENDATIONS
TO THE PARLIAMENT OF CANADA

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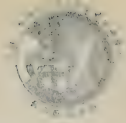


1 The present patchwork of our tax laws is complicated
2 and results in too much effort being utilized in tax
3 avoidance. In connection with income, the thin line
4 between ordinary income and capital gains is often the
5 subject of confusion and dispute. While we appreciate
6 that it may be difficult to avoid a complicated tax
7 structure in a modern industrial state, we nevertheless
8 believe a determined effort should be made to simplify
9 the operation of the tax system as much as possible.
10 The simpler the taxation system, the easier it will be
11 for individuals and business to make decisions without
12 undue emphasis being placed on the tax consequences.
13 It will also be easier to collect taxes on an economical
14 basis.

15 15. The complications resulting from the
16 provisions of the Canadian Income Tax Act are frequently
17 referred to as providing considerable employment to the
18 legal and accounting professions.

19 A more Equitable Distribution of Taxes

20 16. In the relatively brief time available to
21 us to examine the Canadian tax structure we have been
22 impressed by the lack of incentive planning in the tax
23 structure, along with the degree of discrimination that
24 exists against certain segments of the productive
25 population. Examples of inequities are to be found in
26 the various forms of double taxation as income is
27 funnelled through corporate channels to the investor.
28 Another much discussed and little understood example of
29 inequitable distribution of the tax load is that of the
30 agreement among a community of individuals, trading



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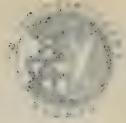
A more equitable distribution of taxes

16. In the examination of the Canadian tax structure we have been impressed by the lack of incentive planning in the tax structure, along with the degree of discrimination that exists against certain segments of the productive population. Examples of inequities are to be found in the various forms of double taxation as income is funnelled through corporate channels to the investor. The inequitable distribution of the tax load is that of the agreement among a community of individuals, trading



1 amongst each other, to reduce their net incomes (and,
2 therefore, their taxable incomes) through the exchanges
3 of goods and services at prices below the then current
4 market prices. Examples of the formal organization of
5 such groups or communities trading among themselves are
6 the phenomena known in Canada as co-operatives or credit
7 unions. Quite apart from whether or not these organ-
8 izations qualify under the Income Tax Act as taxable
9 or tax-exempt (and it has been widely thought that
10 co-operatives are not taxable whereas in fact most of
11 them are taxable), the fact is that such organizations,
12 by expressly reducing their taxable incomes and thereby
13 failing to contribute their fair share of the tax
14 load, illustrate another weakness in the fabric of our
15 income tax structure.

16 17. It is our belief that a modest reduction
17 in the higher marginal rates of personal taxation
18 would be a constructive move and would increase personal
19 incentive and initiative and would at the same time
20 have an almost negligible effect on the revenue of the
21 government. While of course there are always many
22 exceptions, generally speaking we believe that such high
23 marginal rates of personal taxation tend to stifle
24 incentive for hard work and ideas. We question, for
25 example, whether it is right and just for an individual
26 taxpayer to be taxed at a higher rate than the largest
27 Canadian corporations. The highest marginal rates of
28 personal tax (which rise to as high as 80 per cent at
29 the top level) contribute little in relation to the total
30 personal tax dollars collected. If, for instance, the



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1 highest rates of personal tax were limited to 50 per
2 cent (assuming all other rates were to remain as at
3 present), the total loss of revenue to the government
4 would be in the neighbourhood of around \$10,000,000, or
5 substantially less than one per cent of the total
6 personal tax collected. All present trends point to
7 increased political demands on government at all levels
8 to increase public spending for such collective goals
9 as counter-cyclical fiscal policy, education and social
10 welfare. It is obvious that an excessively high rate
11 of income tax tends to decrease the enthusiasm of a
12 high income earner for hard work. The productivity
13 of such a high income earner tends, as a result, to
14 decline as income rises.

15 18. In view of Canada's position, balanced
16 between two huge economic blocks, it is our opinion that
17 it is more important than ever before to encourage and
18 foster within the country individuals having a high
19 degree of ability and to assure that their financial
20 rewards will be greater than is currently the case.
21 This is especially true in certain lines of endeavour,
22 such as the professions and some segments of the service
23 industries, where any material amount of compensation
24 except through salary is essentially impossible.

25 Use of Indirect Taxation

26 19. We are of the opinion that serious
27 consideration should be given to broadening the tax base.
28 For the year 1959, of the approximately 4,200,000
29 personal income taxpayers in Canada, approximately
30 4,000,000 -- or over 95 per cent -- paid less than the



rates of personal tax were limited to 50 per cent (assuming all other rates were to remain as at present), the total loss of revenue to the government would be in the neighbourhood of around \$10,000,000, or substantially less than one per cent of the total personal tax collected. All present trends point to increased political demands on government at all levels to increase public spending for such collective goals as counter-cyclical fiscal policy, education and social welfare. It is obvious that an excessively high rate of income tax tends to decrease the enthusiasm of a high income earner for hard work. The productivity of such a high income earner tends, as a result, to decline as income rises.

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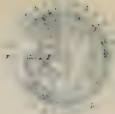
19. We are of the opinion that serious consideration should be given to broadening the tax base for the year 1959, of the approximately \$200,000 personal income taxpayers in Canada, approximately 4,000,000 -- or over 95 per cent -- paid less than the



1 average rate that would have had to be levied against
2 all taxable personal income in order to have collected
3 the same amount of revenue. Such average rate of tax
4 was approximately $17\frac{1}{2}$ per cent on taxable personal income
5 assessed. The approximately 200,000 taxpayers (less
6 than 5 per cent of the total) who paid more than such
7 average rates provided (for the year 1959) over
8 \$500,000,000 out of the total from all taxpayers of
9 approximately \$1,600,000,000. In other words, less
10 than 5 per cent of the taxpayers were required to pay
11 more than 30 per cent of the total personal income
12 tax collected in order that more than 95 per cent of
13 personal income taxpayers could pay less than the
14 average rate of tax (see Exhibit D).

15 20. If the revenues of the government are
16 to be increased substantially, other than through
17 increased receipts as a result of economic expansion,
18 and without hampering the means by which growth is
19 attained, then it is our belief that this will have to
20 be carried out by broadening the tax base. One of the
21 most practical methods of broadening the tax base is
22 through a greater use of indirect taxation and we
23 believe this approach deserves special investigation.

24 21. A higher sales tax and/or a sales
25 luxury tax on all goods and services might be implemented
26 to the end that both corporate income taxes and personal
27 income taxes might be greatly reduced. It is our
28 suggestion that such a sales tax would be easier and
29 less costly to collect than the present system of
30 income tax, due to being based on the act of a sale



the same amount of revenue. Such average rate of tax was approximately $1\frac{1}{2}$ per cent on taxable personal income than 5 per cent of the total) who paid more than such average rates provided (for the year 1929) over \$500,000 out of the total from all taxpayers of approximately \$1,600,000,000. In other words, less than 5 per cent of the taxpayers were required to pay more than 5 per cent of the total income tax. Tax collected in order that more than 95 per cent of personal income taxpayers could pay less than the average rate of tax (see Exhibit D).

20. If the revenues of the government are to be increased substantially, other than through increased receipts as a result of economic expansion, and without hampering the means by which growth is attained, then it is our belief that this will have to be carried out by broadening the tax base. One of the most practical methods of broadening the tax base is through a greater use of indirect taxation and we

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1 which is easily established. Further, a high sales
2 tax concept would tend to encourage personal saving
3 which would be available for investment in the develop-
4 ment of Canada. Under the present personal income tax
5 concept, personal savings are taxed.

6 22. With regard to the broadening of the tax
7 base, we have also been impressed by the fact that many
8 individuals and groups receive the fruits and benefits
9 of Canadian expenditures, but do not pay their full
10 share for these benefits, although they are well able
11 to do so. For example, it appears to us that the
12 present income tax structure is in many ways inadequately
13 related to the important and financial power of
14 institutional, mutual and other similar corporate
15 entities, together with co-operative entities mentioned
16 earlier, and such corporations may not at this time be
17 bearing a fair proportion of the tax burden. In view of
18 this possible loss of revenue to the government, which
19 results in an added tax burden for other taxpayers,
20 we believe a thorough study should be made of the special
21 tax considerations currently enjoyed by certain corporate
22 entities.

23 To Encourage Economic Activity Through the Use
24 of Tax Incentives

25 23. Although all taxation is punitive and
26 acts as a disincentive, nevertheless by varying the
27 emphasis of the tax burden, economic activity and human
28 endeavour can be encouraged to flow in certain directions
29 considered to be desirable. This function of the
30 taxation system in influencing economic objectives by



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To Encourage Economic Activity Through the Use of Tax Incentives

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1 providing direction is one which we believe requires
2 much study. In the consideration of Canada's current
3 and potential problems several areas are indicated
4 where activity and effort might well be encouraged
5 through a positive use of the tax structure to achieve
6 and encourage a strong sense of direction. Particularly
7 is there a need to increase Canadian exports, especially
8 those of manufactured or semi-manufactured goods, and
9 to encourage their distribution throughout a greater
10 number of trading areas. Also of imminent concern
11 is the need to provide for the employment of a labour
12 force that is expanding at a rate considerably in
13 excess of that at which it can be absorbed by existing
14 industry. Neither of the above mentioned problems lend
15 themselves to any easy solution but both requires
16 immediate attention. In our opinion, one method of
17 applying the incentive necessary to encourage activity
18 to move in the direction in which these problems can
19 be solved, or at least alleviated, is through allowing
20 industry to charge depreciation in excess of 100 per
21 cent under certain conditions. An incentive of fairly
22 large proportions must be granted to industry to assure
23 that movement in the desired direction actually will take
24 place. We commend the thinking that under certain
25 conditions industry might be permitted to charge
26 depreciation of as much as 150 per cent to 200 per cent
27 on certain of their assets. In connection with the
28 matter of depreciation, it is interesting to note that
29 Canada continues to use the more complicated reducing
30 balance method of depreciation, while Great Britain has



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1 reverted to the simpler straight line method. This we
2 believe to be another area which requires study.

3 Comparison of Canada's Tax System to Other Countries

4 24. A number of countries, such as Australia,
5 New Zealand, South Africa and the Scandinavian countries,
6 to mention a few, have many of the same basic problems
7 that affect Canada at the present time. In some of
8 these countries, as in Canada, exports of a small number
9 of primary natural resource commodities are extremely
10 important from the point of view of over-all national
11 prosperity. We believe that consideration should be
12 given to the way in which these countries have adapted
13 and oriented their tax structure in order to suit
14 conditions which bear a high degree of similarity to
15 conditions in Canada. These tax structures should
16 also be examined to find out if and what tax incentives
17 are provided to encourage the formation of a strong and
18 prosperous secondary industry. Other countries, such
19 as Sweden, are popularly known as "welfare states" and
20 some examination should be made as to the financing of
21 these welfare benefits. We have noted with interest that
22 the Swedish government appears to be giving increased
23 recognition to the need to broaden the tax base by the
24 recent increase in their national retail sales tax.
25 Mention has already been made herein of the desirability
26 of broadening the tax base in Canada.

27 Tax Problems Related to Corporate Surplus

28 25. Problems relating to corporate taxation
29 are in many respects more difficult of satisfactory
30 solution than those relating to personal taxation. One



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1 of the major corporate tax problems existing today
2 concerns the handling of the various types of corporate
3 surplus for taxation purposes. We understand that a
4 great deal of consideration has been given to this
5 problem by the Department of Finance in Ottawa. While
6 Section 95 and later Section 105 of the Income Tax Act
7 gave some initial relief and encouraged surplus
8 distribution, these sections are unfortunately now
9 relatively cumbersome and ineffective. This has resulted
10 in what we consider to be a wasteful expenditure of
11 time and energy in legal manoeuvres to avoid the current
12 restrictions governing corporate surpluses. We do not
13 wish to suggest that we have any solution for this highly
14 complex problem but we do believe that it might be
15 fruitful to pursue thinking which would result in a
16 basic corporate tax at a fixed rate with a further flat
17 tax being made at the corporate level on all distribut-
18 ions to shareholders, such distributions then being
19 tax free in the hands of the shareholder. We have not
20 been able to follow such a proposal through to its
21 logical conclusion in order to assess all the effects
22 that it would have throughout the economic system.
23 However, it is our understanding that this type of tax
24 is used in a number of countries and the results of its
25 practical operation should be worthy of study.

26 The Effects of Double Taxation

27 26. The dividend tax credit is a most forward
28 and progressive piece of fiscal thinking on the part of
29 government. This legislation was originally passed for
30 the purpose of relieving the effects of double taxation



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The Effects of Double Taxation

26. The dividend tax credit is a most forward and progressive piece of fiscal thinking on the part of Government. This legislation was originally passed for the purpose of relieving the effects of double taxation



1 on the corporate dollar paid out in the form of dividends
2 to shareholders. In 1953, when this dividend tax
3 credit was increased to its present level of 20 per
4 cent, it was also stated that an additional purpose
5 was to encourage Canadians to invest in Canadian equities.

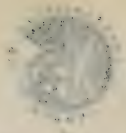
6 27. While the dividend tax credit has gone
7 a long way in relieving the effect of taxing twice the
8 same corporate dollar paid out in dividends, the relief
9 has nonetheless not been completed and it should be
10 recognized that many shareholders continue to carry
11 more than their fair share of the tax burden.

12 The Taxation Effect on Financing

13 28. The use of the dividend tax credit has
14 been successful in encouraging Canadians to invest in
15 Canadian equities as opposed to investing in foreign
16 equities. However, such tax credit has had little
17 apparent effect on encouraging corporations to finance
18 through the issue of equity rather than debt securities,
19 and if this is to be accomplished it would seem that
20 some incentive will have to be given at the corporate
21 level as well as to the shareholder.

22 Differentiation Between Income and Capital Gains

23 29. Undoubtedly in any full study of the
24 existing Canadian tax structure the question of the
25 advisability of instituting a capital gains tax will
26 arise. We have attempted to keep an open mind on this
27 matter of the taxation of capital gains. Such a tax has
28 been in operation in the United States for some years
29 and currently a speculative gains tax is being considered
30 in Great Britain. At the present time in Canada both



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and currently a speculative gains tax is being considered
in Great Britain. At the present time in Canada both



1 the operations of business and of individuals are
2 frequently made more difficult in that there are
3 circumstances under which it is difficult to determine
4 whether such operations are in the area of income or in
5 that relating to capital gains. We realize that the
6 differentiation between these two areas is frequently
7 exceedingly difficult but a more precise definition of
8 each would undoubtedly be of great assistance. We have
9 found no support for a capital gains tax as it exists
10 in the United States, nor do we support such a tax
11 ourselves. Taxation of capital gains causes at times
12 severe market dislocations, as individuals and corp-
13 orations sell for the purpose of establishing capital
14 losses to apply against capital profits. Such artificial
15 effects on the market are not in the public interest.
16 Furthermore, such a tax has the disadvantage of having
17 a high cost of calculation and collection. The
18 requirement of the Canadian economy for continuing and
19 substantial growth in which ever increasing quantities
20 of equity capital is essential indicates that any
21 capital gains tax would be inadvisable and not in the
22 best interests of Canada.

23 Advance Tax Rulings

24 30. In conjunction with the problem of
25 differentiating between capital gains and income, as well
26 as in connection with such other problems as those
27 relating to corporate surpluses, we believe thorough
28 study should be given to enabling a taxpayer to obtain
29 a tax ruling prior to completion of a transaction. This
30 is common practice in the United States and the adoption



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Advance Tax Rulings

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1 of such a policy in Canada would contribute greatly
2 to the elimination of much of the present confusion
3 involved in many business transactions.

4 The Elimination of Tax Disadvantages in Development
5 of Canada's Natural Resources

6 31. The unfavourable position of individuals
7 in Canada who are engaged in the exploration for oil and
8 gas natural resources in Canada, compared to the
9 position of individuals in the United States operating
10 in Canada, is well known and it is believed that
11 numerous submissions have been made to the Department of
12 Finance and Income Tax Department relating to this
13 unfavourable treatment. In effect the United States
14 tax laws permit an individual to write off, against
15 other taxable income, losses incurred in the development
16 of such natural resources. The Canadian tax law
17 does not permit the Canadian individual this type of
18 write-off and it may well be due to this reason that such
19 a high percentage of such Canadian natural resources are
20 foreign controlled. While we do not agree or disagree
21 with these laws as they are applied in the United States,
22 the effect of the Canadian law has not been beneficial
23 to Canada, and in fact we believe it to have been
24 harmful.

25 Revision of the Tax System for the Orderly
26 Growth of the Economy

27 32. Perhaps one of the most distressing of
28 all the features that can be attributed to the present
29 tax structure is that in a period when the need for
30 fiscal controls as an aid in regulating the economy is
pronounced, the use of our tax structure as a fiscal



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The Elimination of Tax Disadvantages in Development
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Revelation of the Tax System for the Growth of the Economy

32. Perhaps one of the most distressing of all the features that can be attributed to the present tax structure is that in a period when the need for fiscal controls as an aid in regulating the economy is pronounced, the use of our tax structure as a fiscal



1 agent seems to be impractical from a political point of
2 view. Governments have been prepared to raise taxes in
3 boom years as a brake against inflationary pressures,
4 but have been less prepared to lower taxes during periods
5 of reduced economic activity. It seems likely that
6 because of its lack of political popularity, such a
7 fiscal weapon, effective as it might prove, will rarely
8 ever be used properly or quickly enough, whether for
9 the purpose of stimulation or suppression. The
10 extensive use of indirect taxation would permit rapid
11 controllable changes in our taxation system.

12 33. It has been our intention throughout
13 this brief to point out numerous areas where we believe
14 the current tax structure is hindering rather than
15 promoting economic growth, and at the same time
16 minimizing rather than maximizing government revenues.
17 It has been impossible for us to ascertain in such a
18 brief study where the solution to these problems lies.
19 However, we do believe it essential that the tax
20 structure be more closely linked with a national sense
21 of direction and priorities. Thus we contend that an
22 effort must be made to find a positive approach to
23 taxation that will accomplish far more than the negative
24 approach which currently is employed.

25 34. In order that many of our suggestions may
26 be carried out, a sweeping revision of the present Income
27 Tax Act will be required. We appreciate that many
28 problems will be created in accomplishing this, such as
29 the time and expense in examining our Income Tax Act
30 in its entirety, and the possible nullification of many



boom years as a brake against inflationary pressures, but have been less prepared to lower taxes during periods of recession. It is true that such a policy, because of its lack of political popularity, such a fiscal weapon, effective as it might prove, will rarely ever be used properly or quickly enough, whether for the purpose of stimulation or suppression. The extensive use of indirect taxation would permit rapid expansion of the tax base. This brief to point out numerous areas where we believe the current tax structure is hindering rather than promoting economic growth, and at the same time maintaining a high level of living. It has been impossible for us to ascertain in such a brief study where the solution to these problems lies. However, we do believe it essential that the tax structure be more closely linked with a national sense of direction and priorities. Thus we contend that an effort must be made to find a positive approach to taxation that will accomplish far more than the negative approach which currently is employed.

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1 established legal decisions. Nevertheless, in
2 consideration of the impact taxes have on Canada's
3 economy, it appears essential that competent personnel
4 should carefully study, and recommend revision in, our
5 tax laws so as to assist in the continued development of
6 Canada.

7 Conclusions and Recommendations

8 35. Any review of the tax structure of a
9 complex industrialized society requires a detailed
10 appreciation of the impact that taxes have on the
11 economy; on long term economic development; and even
12 on the formation of social attitudes and national out-
13 look. In the time available for the preparation of
14 this brief it has been impossible to approach the
15 subject of taxation in the detail and depth which is
16 needed, and which in our opinion is urgently required.
17 Therefore, we have tended to confine our study of
18 taxation in Canada to those areas where we feel a
19 revision of the existing tax structure would be of
20 greatest benefit to all Canadians and to express our
21 conclusions in relatively general terms.

22 1. In general, we have concluded as follows:

23 i. Greatly increased government spending
24 in recent years has necessitated greatly
25 increased taxation. The political
26 inclination for increased government
27 spending seems likely to continue. We
28 question whether the income tax path
29 and our income tax structure is the
30 best available means of meeting such

Paras.
1 to 6
incl.



Conclusions and Recommendations

35. Any review of the tax structure of a complex industrialized society requires a detailed appreciation of the impact that taxes have on the economy; on long term economic development; and even on the formation of social attitudes and national outlook. In the time available for the preparation of this brief it has been impossible to approach the subject of taxation in the detail and depth which is needed, and which in our opinion is urgently required. Therefore, we have tended to confine our study of taxation in Canada to those areas where we feel a revision of the existing tax structure would be of greatest benefit to all Canadians and to express our conclusions in relatively general terms.

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1. Greatly increased government spending in recent years has necessitated greatly increased taxation. The political inclination for increased government spending seems likely to continue. We question whether the income tax path and our income tax structure is the best available means of meeting such



- 1 continuing need for increased revenues.
- 2 ii. There are twelve specific areas Paras.
3 that we feel merit intensive study. In 7 to 10
4 addition , the reports of other studies incl.
5 merit consideration.
- 6 iii. Changes in conditions, particularly
- 7 Canada's position in the world economy, Paras.
8 raise the question as to whether a 11 to 13
9 revised tax structure would not better incl.
10 suit Canada's economic needs.
- 11 iv. The simplification of the tax system, Paras.
12 if possible, would be very desirable. 14 & 15
- 13 v. Inequities in the tax load suggest
- 14 that the present income tax pattern is Paras.
15 less than satisfactory and discourages 16 to 18
16 incentive. incl.
- 17 vi. Indirect taxation should receive
- 18 consideration as an alternative or Paras.
19 partial alternative to income tax. 19 to 22
20 incl.
- 21 vii. An incentive method of applying
- 22 whatever taxation is necessary should Para.
23 receive more attention. 23
- 24 viii. Tax systems of other countries
- 25 should be studied with a view to Para.
26 obtaining ideas for use in Canada. 24
- 27 ix. Tax on corporate surplus should be Para.
28 revised to prevent present inequities and 25
29 unnecessary corporate manoeuvres.
- 30 x. The 20 per cent tax credit has
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if possible, would be very desirable.

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revised to prevent present inequities and

x. The 20 per cent tax credit has

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1 reduction of double taxation in its Paras.
2 various forms should be studied. 26 & 27

3 xi. Use of the dividend tax credit Para.
4 has provided little stimulus to corporate 28
5 equity financing.

6 xii. The requirement of the Canadian
7 economy for continuing and substantial Para.
8 growth in which ever increasing 29.

9 quantities of equity capital is essen-
10 tial indicates that any capital gains
11 tax would be inadvisable and not in
12 the best interests of Canada. Para.
13 30

14 xiii. The advantages of enabling a
15 taxpayer to obtain a tax ruling prior
16 to a transaction merit thorough study.

17 xiv. Canadians are still at a dis-
18 advantage, compared to U.S. citizens Para.
19 and corporations, in respect to the 31
20 development of their own oil and gas
21 natural resources.

22 xv. The use of the present tax
23 structure as a fiscal control in the Paras.
24 orderly growth of the economy has not 32 to 34
25 been properly utilized. In this and incl.
26 other respects taxes must be more
27 clearly linked to a national sense of
28 direction.

29 2. Specifically we recommend the following:

30 i. In order to encourage a more rapid and sound
development of the Canadian economy and to make



Page 26 & 27

various forms should be studied.

xi. Use of the dividend tax credit
has provided little stimulus to corporate

equity financing.

xii. The reduction of the corporate

economy for continuing and substantial

growth in which even increasing

quantities of equity capital as essen-

tial indicates that any capital gains

tax would be inadvisable and not in

the best interests of Canada.
Para. 30

xiii. The advantages of enabling a

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advantage, compared to U.S. citizens
Para. 31

and corporations, in respect to the

development of their own oil and gas

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structure as a fiscal control in the
orderly growth of the economy has not
Para. 32 to 34
been properly utilized. In this and
other respects taxes must be more
clearly linked to a national sense of

Recommendations

Specifically we recommend the following:

1. In order to encourage a more rapid and sound development of the Canadian economy and to make



1 more certain of its ability to absorb a rapidly
2 increasing work force, we recommend the formation
3 of a Select Committee to study and assess the
4 entire tax structure of Canada with the objective
5 of devising an improved taxation system better
6 able to meet Canada's economic needs.

7 ii. We further recommend that before holding
8 public hearings such Select Committee should
9 carry out its initial deliberations on a
10 confidential basis at the highest level in order
11 to arrive at some definite conclusions under
12 objective conditions.

13 iii. Furthermore, such Select Committee should
14 be composed of highly qualified individuals
15 having a broad working knowledge of the present
16 tax structure with most emphasis being placed
17 on its practical operation in business and in
18 the economy as opposed to its legal and account
19 operation. Such a committee should be composed
20 primarily of representatives of Business form
21 members of The Canadian Chamber of Commerce and
22 Boards of Trade, representatives of Finance
23 from members of The Investment Dealers' Association
24 of Canada and The Canadian Bankers' Association,
25 practical economists, and representatives of the
26 Canadian Tax Foundation, and secondarily of
27 members of the Legal and Accounting professions.



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able to meet Canada's economic needs.

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public hearings such Select Committee should
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from members of The Investment Dealers' Association
of Canada and The Canadian Bankers' Association,
practical economists, and representatives of the
Canadian Tax Foundation, and secondary of
members of the legal and accounting professions.

EXHIBIT A

Total Government Revenue Expressed as a Percentage of

Gross National Product

For Selected Calendar Years, 1929 to 1960

Year	Total Government Revenue			Percentage of Gross National Product			Total Taxes (all Governments) as a Per- centage of Government Revenues
	Federal \$mm	Provincial \$mm	Municipal \$mm	Federal %	Provincial %	Municipal %	
1929	399	200	366	6.5	3.3	6.0	13.1
1933	248	167	327	7.1	4.8	9.3	18.5
1939	459	295	356	8.1	5.2	6.3	16.7
1945	2,438	435	396	20.6	3.7	3.3	22.6
1946	2,602	519	417	22.0	4.4	3.5	24.9
1947	2,740	674	455	20.8	5.1	3.5	24.9
1948	2,677	812	511	17.7	5.4	3.4	22.1
1949	2,654	887	556	16.2	5.4	3.4	20.8
1950	2,965	978	624	16.5	5.4	3.5	25.4
1951	4,110	715	715	19.4	5.4	3.4	23.8
1952	4,626	1,136	809	19.3	4.7	3.4	23.0
1953	4,726	1,188	874	18.9	4.7	3.5	22.7
1954	4,528	1,246	945	18.2	5.0	3.8	22.3
1955	4,937	1,409	1,040	18.2	5.2	3.8	22.5
1956	5,578	1,598	1,163	18.2	5.2	3.8	22.6
1957	5,588	1,877	1,288	17.5	5.9	4.0	22.7
1958	5,321	1,979	1,416	16.2	6.0	4.3	21.7
1959	6,005	2,226	1,549	17.2	6.4	4.4	23.1
1960	6,280	2,354	1,672	17.5	6.5	4.6	23.4

Exclusive of inter-governmental transfers.

Includes Newfoundland for 1949 and subsequent years.

(All dollar figures stated in millions)

Source: NATIONAL ACCOUNTS, INCOME AND EXPENDITURE, D.B.S. (Dollar Figures Only).

REPORT V

Department of Agriculture

[illegible]

and as everyone knows, Isador
Dobson would do anything

[illegible][illegible]

• *Список литературы, относя к разделу*
• *«Воспитание детей в семье»*

(unofficially not a "solid line")



EXHIBIT B

A few of the many comments by prominent Canadians
on the Tax Structure

The high levels of taxation and the discouragement of incentive through the incidence of taxation impede the accumulation of risk-taking capital which will be necessary for our future growth.

Neil J. McKinnon,
President,
Canadian Imperial Bank of
Commerce,
December 12, 1961.

There is, however, one aspect of our cost structure which will remain to plague us in spite of any progress we may make in our efforts to increase the efficiency of industry: I refer to our dis-incentive tax structure.

The burden of taxation lies not only in its absolute level, or even in its level relative to other countries, but in distortions induced by the uneven incidence of taxation. Greater incentive, and a greater national product, require a reform of our personal income tax, our corporate income tax, and our whole system of sales and excise taxes, with incentive as one, though by no means of course the only, object in view.

W. Earle McLaughlin,
President,
The Royal Bank of Canada,
January 11, 1962.

Counting all forms of taxes and exemptions, there is no question that the burden of taxation in Canada for the technical, professional and supervisory groups is



A Plan of the Royal Bank of Canada
on the Tax Structure

The main levels of taxation and the discouragement
of investment through the incidence of taxation impedes
the development of a more efficient and balanced
economy for the future.

Presented to the
Board of Directors,
The Royal Bank of Canada
December 12, 1961.

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structure which will remain to plague us in spite of any
progress we may make in our efforts to increase the
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absolute level, or even in its level relative to other
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greater national product, require a reform of our
personal income tax, our corporate income tax, and our
whole system of sales and excise taxes, with incentive
as one, though by no means of course the only, object
in view.

Presented to the
Board of Directors,
The Royal Bank of Canada,
January 11, 1962.

Existing all forms of taxes and exemptions, there
is a question that the burden of taxation in Canada for
the individual, particularly the individual taxpayer, is



Nethercut & Young
Toronto, Ontario

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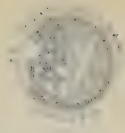
1 far more onerous than elsewhere on this continent.
2 It is little wonder, therefore, that we continue to
3 lose thousands of our best trained Canadian men and
4 women to the United States and elsewhere, and are left
5 with more and more untrained unemployables to look after.
6 Unless there is more incentive for educated Canadians to
7 stay here and for skilled outsiders to come to Canada
8 and remain, it will be very difficult for us to have a
9 buoyant and expanding economy. We shall lose the very
10 people who could and would make Canada great. I suggest
11 that this incentive should be provided by reducing our
12 present tax ~~loans~~ so that they are definitely more
13 favourable than elsewhere on this continent, and when
14 we have done that we should live within our means.

15 This, of course, implies that we should give much
16 careful study and consideration to our present heavy
17 burden of welfare costs and subsidies before increasing
18 present commitments or embarking on new programs, as
19 desirable as many of them seem to be.

20 E.G. Burton,
21 Chairman and President,
22 Simpsons, Limited
23 April 25, 1962.

24 Not only is there a need to restrain further
25 increases in the already heavy tax burden, but a complete
26 overhaul of our taxing systems is long overdue and I
27 feel that this should be undertaken without delay.

28 V.W. Scully,
29 President,
30 The Steel Company of Canada,
April 16, 1962.



THE CANADIAN STEEL COMPANY LIMITED

1000 BAYVIEW AVENUE, SCARBOROUGH, ONTARIO

Dear Sirs:

Reference is made to your letter of the 14th inst.

concerning the proposed increase in the tax on

imported steel.

It is noted that you are of the opinion that

the proposed increase will be detrimental to the

Canadian steel industry.

We are sorry to hear of this and would like to

point out that the proposed increase is not

intended to be a punitive measure.

It is our hope that the proposed increase will

be a temporary measure.

We are sure that you will understand our

position.

Very truly yours,

Chairman and President,

Canadian Steel Industry Association

1000 BAYVIEW AVENUE, SCARBOROUGH, ONTARIO

April 25, 1962.

Enclosed for you are two copies of a letter

from the Canadian Steel Industry Association

dated April 16, 1962.

Very truly yours,

Chairman and President,

Canadian Steel Industry Association

1000 BAYVIEW AVENUE, SCARBOROUGH, ONTARIO

April 16, 1962.

Enclosed for you are two copies of a letter

from the Canadian Steel Industry Association



1 Extract from The Financial Post, May 5, 1962.

2 NATION'S BUSINESS

3 Why Do They Avoid Issues that Count

4 To judge by the droves and herds of pollsters,
5 admen, image-makers and assorted pseudo-scientific experts
6 running the campaigns of all political parties, we are
7 entering the final stages of the most researched and
8 systematically organized general election in this
9 country's history.

10 But it is remarkable, indeed, when the vast majority
11 of adult Canadians have just filed tax returns that not
12 a single politician has excoriated Canada's iniquitous
13 and hare-brained tax structure, and that there is no
14 significant public discussion of our vicious and
15 punitive tax rates.

16 All major contenders for this country's highest
17 offices have made national growth the central theme of
18 their platforms -- yet all ignore the fact that the tax
19 burden in Canada is one of the heaviest in the world.
20 This is a preposterous state of affairs in a still-
21 maturing nation and in one of the nations where
22 individuals making their own decisions and left with
23 their own money to invest in their plans and in their
24 dreams can make for the greatest national growth.

25 Soak-the-rich taxation is no sensible basis for
26 running the Canadian economy. We have slow national
27 growth because we lack a high rate of capital investment.
28 Yet very few can save when excessive tax rates leave
29 little incentive and who will invest when worthwhile
30 rewards are absent?



Statement of the Hon. J. G. ...
Minister of Finance
in the House of Commons

To Judge by the groves and herds of pollsters,
admen, image-makers and assorted pseudo-scientific experts
running the campaigns of all political parties, we are
entering the final stages of the most researched and
sustainedly executed political election in this
country's history.

But it is remarkable, indeed, when the vast majority
of adult Canadians have just filed tax returns that not
a single politician has excoriated Canada's intricate
and hare-brained tax structure, and that there is no
significant public discussion of our vicious and
punitive tax rates.

All major contenders for this country's highest
offices have made national growth the central theme of
their platforms -- yet all ignore the fact that the tax
burden in Canada is one of the heaviest in the world.
This is a preposterous state of affairs in a still-
maturing nation and in one of the nations where

individuals making their own decisions and left with
their own money to invest in their plans and in their
dreams can make for the greatest national growth.
Look-the-rich taxation is no sensible basis for
running the Canadian economy. We have slow national
growth because we lack a high rate of capital investment.
Yet very few can save when excessive tax rates leave
little incentive and who will invest when worthwhile



1 The old-time philosophical justification for
2 violently progressive taxation is now greatly weakened.
3 Three decades of punitive levies have scaled down old
4 inherited fortunes and hastened the great sell-out of
5 Canadian companies to foreign control. Few are without
6 cars, fewer still without TV sets and fewer still
7 without adequate food.

8 It is now the high earners who are being soaked --
9 precisely those Canadians who possess initiative,
10 accomplishment and enterprise; the roots of our society.
11 Indeed, taxation has so reached down, and inflation has
12 so pushed up incomes that an important portion of the
13 nation's resources of intelligence is spent devising
14 schemes to minimize taxes, schemes that make no
15 contribution to the productiveness of the economy.

16 What our tax system should do is unleash
17 existing talent in Canada and attract new talent of
18 all kinds. It should not punish enterprise. It should
19 reward energy and innovation.

20 If Canada is to prosper as an independent nation
21 and if we are to retain the benefits of individual
22 initiative, then our leaders must find the political
23 courage and the economic sophistication necessary to
24 overhaul our whole approach to taxation and to have
25 the courage to talk this in their campaign speeches.

26 Their present preoccupation with political
27 gimmicks and giveaways will only lead to further economic
28 slowdown and to the further weakening of that great
29 central body of responsible Canadians which gives
30 character to this nation.



The old-time philosophical justification for

violently progressive taxation is now greatly weakened.

These features of positive taxation have caused some of

inherited fortunes and have caused the great selling of

Canadian companies to foreign control. Few are without

cars, fewer still without TV sets and fewer still

without airplanes.

It is now the high earners who are being asked --

precisely those Canadians who possess initiative,

accomplishment and enterprise; the roots of our society.

Indeed, taxation has so reached down, and inflation has

so pruned up incomes that an important portion of the

nation's resources of intelligence is spent devising

schemes to minimize taxes, schemes that take no

contribution to the productivity of the economy.

What our tax system should do is to make

existing talent in Canada and attract new talent of

all kinds. It should not punish enterprise. It should

reward energy and innovation.

If Canada is to prosper as an independent nation

and if we are to retain the benefits of individual

initiative, then our leaders must find the political

courage and the economic sophistication necessary to

overhaul our whole approach to taxation and to have

the courage to talk this in their campaign speeches.

There is no doubt that the political

leadership of the future will be the

central body of responsible Canadians which gives



EXHIBIT C

Merchandise Exports (Dollar Volume)

Millions of Dollars

	<u>Total</u>	<u>To the U.K.</u>	<u>U.K. as % of Total</u>	<u>To the U.S.</u>	<u>U.S. as % of Total</u>
1938	\$ 848.6	\$341.4	40%	\$ 278.7	33%
1960	\$5,405.0	\$923.0	17%	3,043.0	56%

Sources: 1938 Trade of Canada - 1938 (D.B.S.).

1960 Canadian Statistical Review, March 1962. (D.B.S.)

1900 Canadian Statistical Review, March 1905, (D.B.2) (1905)

Source: 1938 Index of Cases - 1938 (D.B.2.).

MILLIONS OF DOLLARS

UNITED STATES DEPARTMENT OF AGRICULTURE

EXHIBIT D

1959 Average Rates of Tax - Gross Income Classifications

<u>Income</u>	<u>Less than \$9,000</u>	<u>More than \$9,000</u>	<u>Total</u>
Number of taxable returns	4,076,921	165,569	4,242,490
Total income assessed	\$ 14,850,205,000	\$ 2,598,084,000	\$ 17,448,289,000
Taxable income assessed	\$ 6,895,993,000	\$ 2,058,156,000	\$ 8,954,149,000
Tax payable	\$ 1,051,166,000	\$ 528,875,000	\$ 1,580,041,000
Average rate of tax (Tax payable as a percentage of taxable income assessed)	15.2%	25.7%	17.6%

<u>Income</u>	<u>8,000 to 8,999</u>	<u>9,000 to 9,999</u>
Taxable income assessed	\$ 335,367,000	\$ 249,198,000
Tax payable	\$ 58,457,000	\$ 44,737,000
Average rate of tax	17.4%	17.9%

Source: 1961 Taxation Statistics, Department of National Revenue

2. Summary

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